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CORPORATIONS
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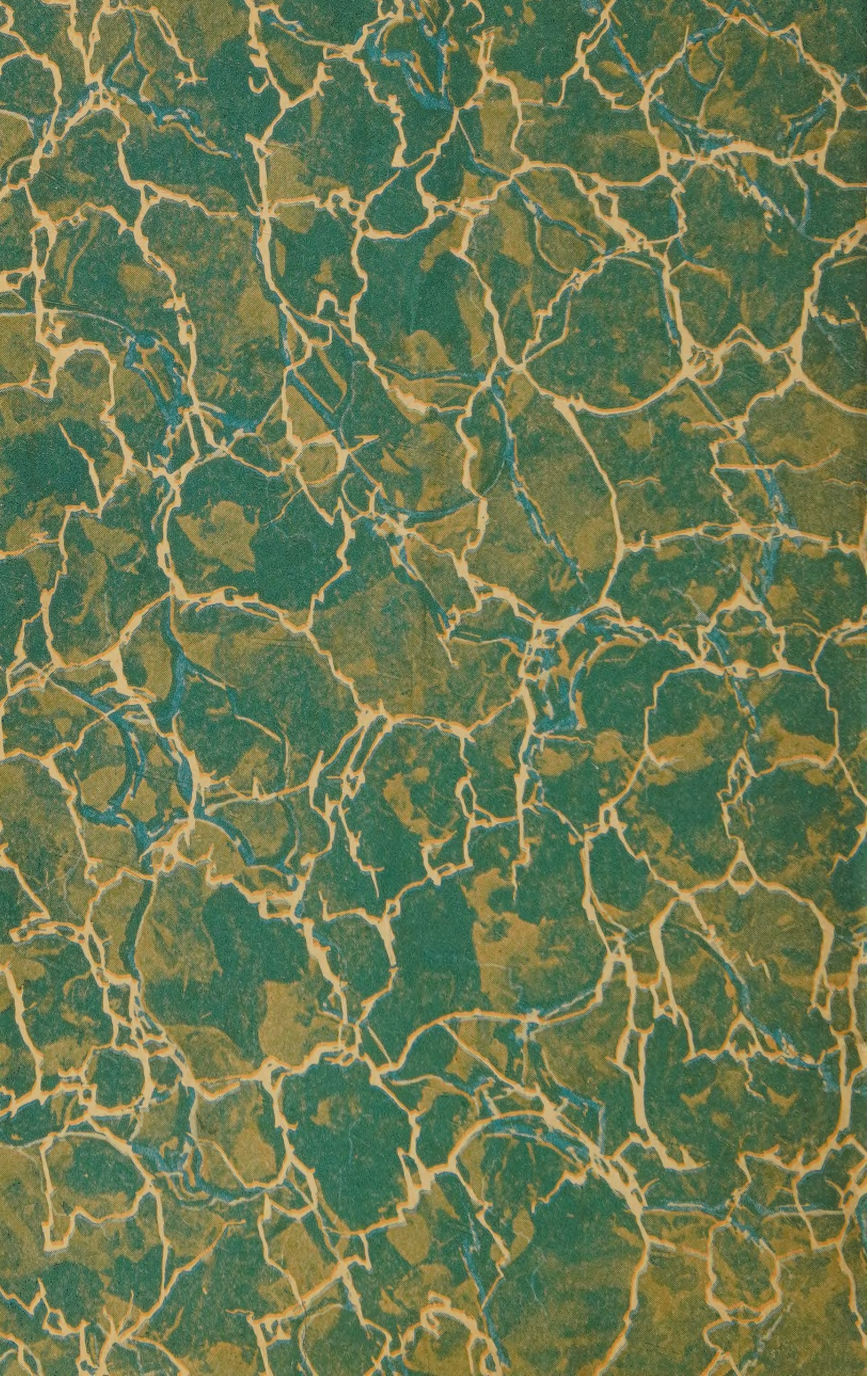

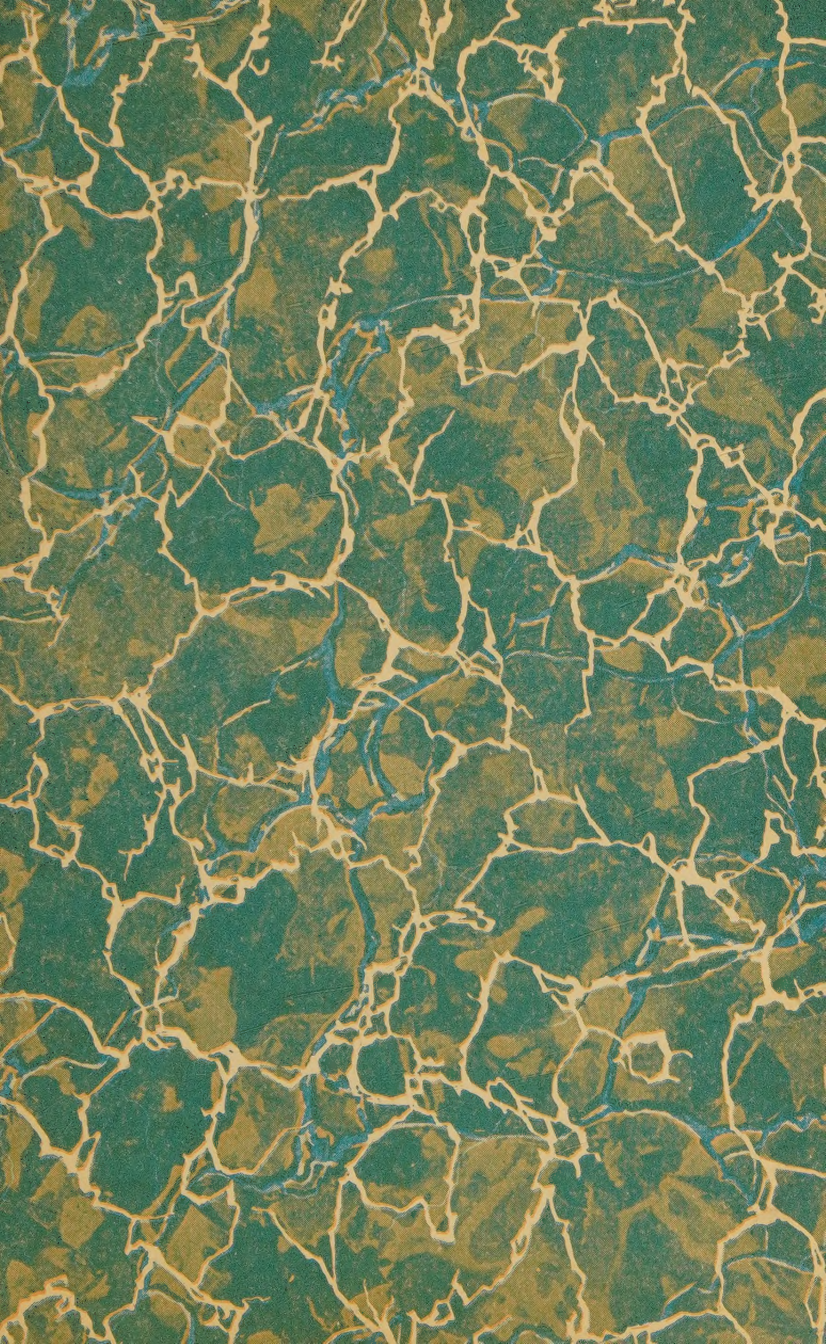

Law—Corporations, Property, Estates

By

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CORPORATIONS
PERSONAL AND REAL PROPERTY
SALES AND MORTGAGE OF PERSONAL PROPERTY
SURETYSHIP AND GUARANTY
MANAGEMENT OF DECEDENTS' ESTATES

93

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AMERICAN BUSINESS LAW

(PART 6)

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CORPORATIONS

FORMATION AND POWERS OF CORPORATIONS

(A) The charter.

1. A corporation is a body consisting of one or more natural or artificial persons, established by law, usually for some specified purpose or purposes, and continued by succession of members. The existence of a corporation is evidenced by a written instrument, usually called the charter or the certificate of incorporation. It has been seen that a partnership is formed by the voluntary agreement of its members. In a corporation, however, in addition to the agreement of the persons forming the corporation, the consent of the state is required. This consent is shown by the charter. The persons who acquire a proprietary interest in a business corporation are called the stockholders. The stockholders choose certain persons as the board of directors to govern and control the corporation. Ordinarily the directors choose the president, the secretary, the treasurer, and other officers to perform certain designated duties in the management of the corporation under the supervision of the board of directors. See Art. **68.**

2. Corporations are either public or private. Public corporations are such as exist for governmental purposes, such as cities, boroughs, and the like. All other corporations are private. Private corporations are divided into two groups: (1) Those formed for the sake of pecuniary profit; and

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(2) those formed for some purpose other than pecuniary profit. Corporations formed for pecuniary profit include tens of thousands of commercial, manufacturing, and mining companies. Corporations not formed for pecuniary profit include most religious, educational, charitable, and social corporations.

3. Corporations which supply public utilities, sometimes known as public service corporations, such as transportation companies, gas companies, and water companies, are called semipublic corporations. They are created by private enterprise, and developed by private capital. They are public in so far as they serve the public generally, and exercise the public right of eminent domain. See Arts. **101-111.**

4. Formerly each new corporation was created by a special act of the legislature. But now, in almost every state, the power of the legislature to form corporations by special act has been taken away, and general laws exist under which a corporation may be formed. Under the general incorporation laws of many states the power of chartering certain corporations is delegated to a judge or some other official.

5. Where a corporation is about to be formed under the laws of any state, generally the procedure is as follows: The first step is to prepare an application for a charter, addressed to the governor, the secretary of state, or some other designated official of the state under whose laws the applicants desire to incorporate. Usually this document sets forth the name of the proposed corporation, the purpose for which it is to be formed, the period during which it is to exist, its principal place of business, the amount of its capital stock, the names and the addresses of the subscribers to the stock, with the amount subscribed for by each, and in some cases the names and the addresses of those who will be its directors for the first year. In most cases the truth of the matters set forth in the application must be verified by the affidavit of one or more of the incorporators. In many states one or more of the incorporators are required to be local residents. In some cases, public notice must be given by advertisement for a certain length of time of the intention to apply for a charter, and of the pur-

pose for which the corporation is to be organized. If the application is in regular form, it is approved and recorded in a designated state office, and the authority to form the organization, called the "letters patent," is issued to the incorporators.

6. A meeting of the incorporators for the acceptance of the charter and the adoption of by-laws is usually the next step in the organization of the company. In some states the directors named in the application are directors for the first year; in most states the election of directors is held at the first meeting of the incorporators. Ordinarily, when the directors hold their first meeting they elect the president and other officers for the coming year. When officers have been chosen, the corporation is ready to proceed with business.

(B) The by-laws.

7. The by-laws of a corporation are the fundamental private regulations by which it is governed. A corporation has power to make by-laws for its own government, provided they are not inconsistent with its charter or with the laws of the United States, or of the state in which the corporation is formed. Usually the consent of a majority of the stockholders is necessary for the original adoption of the by-laws and for any subsequent amendment of them.

The following is a typical form of by-laws:

ARTICLE I

MEETINGS

The stated meetings of the board of directors shall be held on the first Tuesday of every month, at the company's office in Camden, N. J., at 4 P. M., except when the first Tuesday of any month shall fall on a legal holiday, in which case the meeting shall be held on the day following, at the same hour. Special meetings shall be called by the president at the written request of three members.

ARTICLE II

OFFICER

At their first meeting after the annual election, or as soon thereafter as may be convenient, the board of directors shall elect a president, a vice-president, a secretary, a treasurer, a solicitor, and such other officers as may be necessary. The officers shall hold their respective offices only at the pleasure of the board of directors.

ARTICLE III

THE PRESIDENT

The president shall preside at all meetings of the board of directors. He shall appoint all committees not otherwise ordered by the board of directors, and shall be a member of the same *ex officio*. He shall attend to the executive business, and have charge of the general welfare of the company, under the direction of the board of directors. In the absence of the president, the vice-president shall perform his duties.

ARTICLE IV

THE SECRETARY

The secretary shall keep a regular record of the proceedings of the board of directors, give notice to the directors of all stated or special meetings, attend the meetings of all committees, when so required, have the custody of the seal of the company, conduct the correspondence, keep the books of the company, and attend to such other proper duties as the president or the board of directors may require. He shall give at least five days' notice of all annual and special meetings of the stockholders.

ARTICLE V

THE TREASURER

The treasurer shall give bond, with one or more satisfactory sureties, for the faithful performance of his duties, in such sum or sums as the board of directors may from time to time require. He shall keep a separate account in the name of the company in such bank or banks as the board of directors may from time to time designate, and the funds deposited therein shall be subject to drafts or checks, signed by the president and the treasurer. At each stated meeting of the board of directors, the treasurer shall make a detailed report of the receipts and the disbursements, and at the stated meeting in February of each year, he shall present a complete statement of his accounts for the year ending on the previous thirty-first day of December. His books shall be open at all times to the inspection of the president and the board of directors, or any member thereof. All payments shall be made by orders drawn on the treasurer, under appropriations granted by the board of directors, signed by the president and the secretary.

ARTICLE VI

CERTIFICATES OF STOCK

Certificates of stock shall be signed by the president and countersigned by the treasurer, authenticated by the seal of the company and countersigned by the registrar of transfers.

All certificates surrendered shall be canceled by the president and the treasurer, each of whom, at the time of transfer, shall cancel his own signature, or the signature of his predecessor in office. The certificates

so canceled shall be examined and reported on monthly by the finance committee.

ARTICLE VII

COMMITTEES

The standing committees, to be appointed annually on or before the first stated meeting of the board of directors, shall be a finance committee, to consist of three members, and an executive committee, to consist of four members. The standing committees shall hold at least one stated meeting per month, and at all meetings one of the members, or the secretary of the company, shall act as secretary.

The finance committee shall have general supervision of the finances of the company, examine and audit all bills before they are presented to the board of directors for payment, and the certificate book, and report their proceedings to the board of directors at each stated meeting.

The executive committee in conjunction with the president, shall have charge of all matters relating to the company's general welfare.

ARTICLE VIII

ELECTIONS

All elections shall be by ballot, unless by unanimous consent, when a vote may be taken *viva voce*.

ARTICLE IX

OFFICE

The office of the company shall be in the city of Camden, New Jersey, and shall be kept open for the transfer of stock and the transaction of other business, every day (between nine and three o'clock), except Saturday afternoons, Sundays, Good Friday, Christmas, and the fourth day of July, unless otherwise ordered by the board of directors.

ARTICLE X

ORDER OF BUSINESS

At all stated meetings of the board of directors the order of business shall be as follows:

1. A quorum being present, the president shall call the board to order.
2. Roll call.
3. Minutes of the preceding meeting or meetings shall be read, and amended, if necessary.
4. Report of treasurer.
5. Reports of committees.
6. Unfinished business.
7. New business.

ARTICLE XI

AMENDMENTS

No alteration or amendment shall be made to these by-laws, unless presented in writing at a stated meeting of the stockholders, to be acted on at a subsequent stated meeting

(C) Powers of corporations.

8. A corporation has only such powers as are conferred on it by its charter. Powers may be so conferred on a corporation: (1) expressly, by being enumerated in the charter; (2) impliedly, because they are incidental to corporate existence, or because they are necessary or proper for the exercise of the powers expressly conferred. Ordinarily the chief powers of a corporation are as follows: (1) to have succession; (2) to have a corporate seal; (3) to acquire, hold, and dispose of real and personal property suitable to its purposes; (4) to appoint and remove officers and agents; (5) to make by-laws and regulations for its government; (6) to make contracts in furtherance of the objects for which it was created.

9. The power to purchase and hold such real and personal property as the purposes of the corporation may render necessary or proper is an incident of every corporation, unless specially restricted by its charter or by some statute. Generally such power is expressly conferred, but this is not necessary, for it is implied in the absence of an express restriction.

10. Collateral to the power to acquire and hold real estate is the power to sell or mortgage property unless restricted by charter or statute. But not all corporations may mortgage or sell their property. Usually a railroad company or any other corporation that is vested with the power of eminent domain, and charged with peculiar duties to the public, such as telegraph, gas, and water companies, cannot, in the absence of express authority from the legislature, sell, mortgage, or lease property which is essential to enable it properly to perform its functions. See Arts. **101-111.**

11. Except in so far as expressly restricted, a private corporation may borrow money whenever the condition of its business renders this action expedient. Therefore, a corporation has implied power to issue negotiable paper if that is the usual or appropriate way of accomplishing the purposes for which it was created.

(D) Ultra vires acts.

12. When a corporation assumes to do an act which it has no power to do or in excess of the powers which have been conferred upon it, its conduct is said to be *ultra vires,* that is, beyond or in excess of its powers.

13. If neither party has entered upon the performance of an *ultra vires* contract, the courts will not lend their aid to enforce it.

14. If an *ultra vires* contract has been partly performed by one or both parties, most courts will enforce the contract, if this is necessary to do justice. Suppose that a corporation and an individual enter into a contract under which the corporation agrees to perform acts which are in excess of its powers but not otherwise illegal. In most jurisdictions, including Indiana, Michigan, Minnesota, New Jersey, New York, and Pennsylvania, if either party has performed his side of such a contract, the courts will compel performance by the other party should the latter refuse to perform, on the ground that to let the defense of *ultra vires* prevail, would produce an inequitable result.

15. In the Massachusetts and the United States courts it has been held that an *ultra vires* contract is illegal and void, because contrary to public policy. Therefore, even though the individual has performed his part, he cannot hold the corporation liable on the contract. And if the corporation has performed its part of an *ultra vires* contract, the other party may successfully resist the enforcement of the contract by the corporation on the ground that it was beyond the corporate powers. But even in these jurisdictions the rule has been relaxed in the case of a party who was ignorant of the *ultra vires* character of the transaction, and in certain other cases.

16. The rule with respect to the *ultra vires* contracts of municipal corporations is different from that prevailing in the case of private corporations. The courts have generally refused to enforce the *ultra vires* contracts of municipal corporations. Notwithstanding the hardship which a strict

observance of this principle occasions, such contracts are usually declared to be utterly void.

(E) Promoters and contracts made by them.

17. Promoters who have been instrumental in organizing a corporation, and who want to be reimbursed for the services rendered and expenses incurred for its benefit, usually cannot recover from the corporation, unless the stockholders or the directors, by a resolution regularly passed after the organization has been completed, expressly promise to pay.

18. When people deal with the promoters of a corporation before it is organized, they should remember that the corporation is not bound by contracts to which it is not a party, and the promoters cannot be regarded as its agents for the reason that it is not yet formed. In order to secure the benefits of a contract made with promoters before incorporation, one should be careful to have it formally adopted by the company after organization. It will then have the effect of a contract made by the company as of the date of its adoption. Promoters, however, are personally liable on these contracts, unless expressly exempted by the terms thereof.

19. While promoters do not occupy the position of agents for the projected corporation so as to bind it by contracts with third parties, yet as between the promoters and the corporation, they are held to occupy a fiduciary relation, and must display toward it the loyalty which an agent owes to his principal. Accordingly, they are sometimes compelled to pay over to the company any profits made by them in transactions which they have entered into on its behalf.

20. The owner of property may be active in the promotion of a corporation, and afterwards openly sell the property to the company at a fair valuation, without violating his fiduciary obligations. But once he starts upon the promotion of a company, he cannot buy property in order to resell it at an advanced price to the corporation and thereby make a secret profit, without being liable to account for the profit which he makes on the resale.

ADMISSION TO MEMBERSHIP IN A CORPORATION, EXPULSION THEREFROM AND TRANSFER OF INTEREST THEREIN

21. In corporations formed for profit the term "member" usually means a stockholder. Most of the corporations which are not formed for profit have no capital stock, membership in them being largely a matter of personal qualifications.

(A) Membership in corporations not formed for profit.

22. Membership in corporations not formed for profit is usually regulated by the charter and by-laws. The members of a corporation not formed for profit have the right to prescribe any qualifications for membership which do not contravene state or federal laws or public policy.

23. A member of a corporation not formed for profit may lose his right to membership therein, and be liable to suspension or expulsion. Sometimes this occurs through the violation of the rules of the association, as, for example, through nonpayment of dues. Conviction of an infamous crime is usually a ground for expulsion. It may even be that engaging in a specified business may become a cause for expulsion from a corporation not formed for profit.

ELLERBE *v.* FAUST, 119 Mo. 653 (1893). Faust was a member of a Masonic benefit association. This association passed a by-law providing that if any member were to become a saloon-keeper, he should forfeit his membership and all benefits. *Held* that as Faust kept a saloon after the passage of the by-law, he came within its operation, and lost his membership in the association without any formal action on its part.

(B) Membership in corporations formed for profit.

24. The capital stock of a business corporation is the money or other property which is put into a fund by those who become members of the concern. It is the means contributed by the stockholders as the basis of the business enterprise for which the corporation was formed. The interest which each member has in the corporation, namely, the right to participate

in profits, and upon dissolution to participate in the division of assets, is called his share, or shares, of stock. Members of business corporations are called shareholders or stockholders. Sometimes a single stockholder acquires all the shares of stock without affecting the corporation's existence.

25. Membership in a business corporation, that is to say, the ownership of shares, is usually evidenced by a certificate issued under the corporate seal. When shares are sold, the certificate, together with a power of attorney to transfer the shares represented by it, is delivered to the purchaser, who turns over both documents to the company. The company then registers the new owner on its books, and issues a new certificate to him. Sometimes the purchaser of stock omits to have the stock transferred to his name on the company's books. Until transfer is made, dividends and notices of stockholders' meetings will be sent to the former owner.

1. Stock Certificates

26. Every stockholder in a corporation is entitled to receive from the company a certificate of the number of shares standing to his credit on the books of the company. This certificate is an acknowledgment by the corporation that the person to whom it was issued is entitled to all the rights of a stockholder in the company in respect of the number of shares named.

27. Fig. 1 is a typical form of stock certificate which constitutes evidence of a shareholder's ownership of a certain interest in the corporation.

28. If the registered owner of stock signs the following power of attorney, engraved on the back of the certificate, without filling in the blanks, and delivers such certificate to a purchaser of the stock, the latter ordinarily surrenders the certificate to the transfer clerk of the corporation which issued it. Then this clerk acts as the seller's agent to transfer the stock, and issues a new certificate to the purchaser. Fig. 2 shows the form of the power of attorney engraved on the back of the stock certificate which appears in Fig. 1. This power of attorney is signed in blank, by Harold Beauchamp,

the person in whose name the stock certificate has been made out.

29. When the shares of stock represented by a certificate are hypothecated as security for a loan, usually it is wiser not

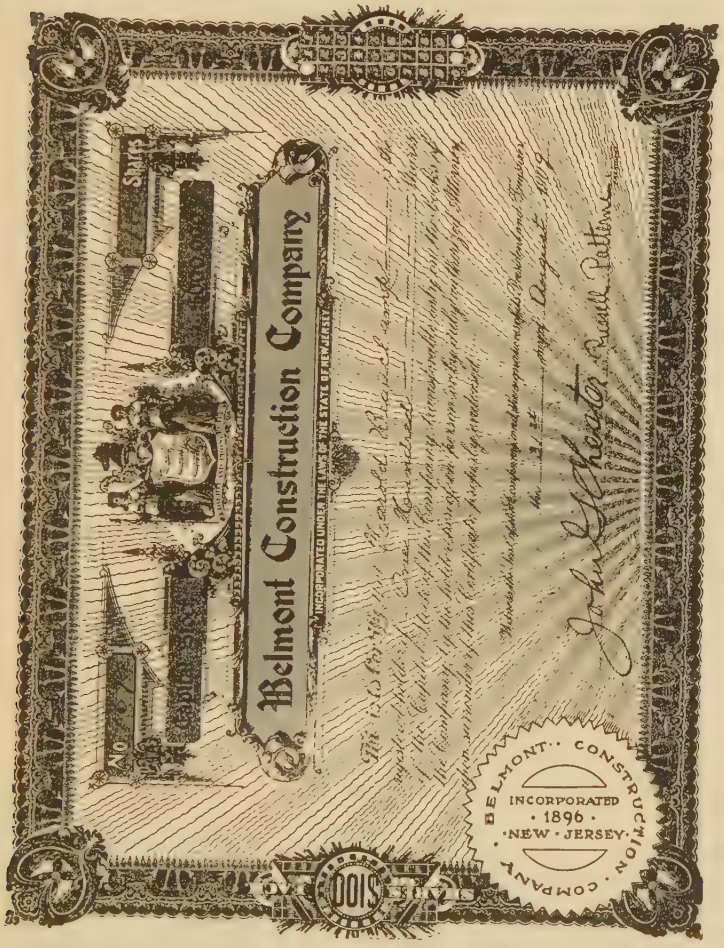
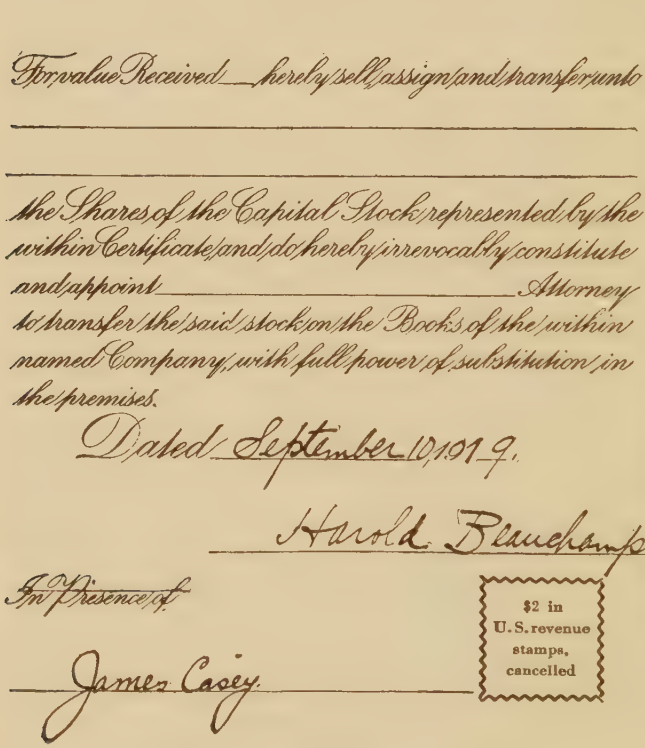


FIG. 1

to sign the form of assignment and power of attorney which appears on the back of the certificate, unless the transfer is to be made at once. It is customary for a stockholder who is

hypothecating his stock as security for a loan to deliver the certificate to the money lender, together with a detached assignment and power of attorney. Then when he pays off the loan he gets back both the certificate and the assignment and power of attorney. He destroys the latter, for it has served its purpose. This is better than to have the form on the


For value Received hereby sell assign and transfer unto

the Shares of the Capital Stock represented by the within Certificate and do hereby irrevocably constitute and appoint Attorney to transfer the said stock on the Books of the within named Company with full power of substitution in the premises.

Dated September 10 1919.

Harold Beauchamp

In Presence of

James Casey

$2 in U.S. revenue stamps, cancelled

NOTICE: THE SIGNATURE TO THIS ASSIGNMENT MUST CORRESPOND WITH THE NAME AS WRITTEN UPON THE FACE OF THE CERTIFICATE, IN EVERY PARTICULAR, WITHOUT ALTERATION OR ENLARGEMENT OR ANY CHANGE WHATEVER.

FIG. 2

back of the certificate signed as indicated in Art. **28,** because in the latter case the certificate would remain negotiable by delivery, and, if stolen and transferred by the thief to a purchaser in good faith, it would be forever lost to the registered holder, Harold Beauchamp. The purchaser in good faith could have himself substituted as the registered holder of the shares in Beauchamp's place. The form shown in Fig. 3 is a

separate assignment and power of attorney to transfer stock which might be used in connection with the certificate shown in Fig. 1.

30. If a stockholder loses his certificate, usually he may have a new one issued to him upon his agreeing to indemnify the company for any loss which may be suffered by the company by reason of the lost certificate, and upon giving proper security.

2. Voting Trusts

31. A voting trust is created when some or all of the stockholders of a corporation transfer their shares in the com-

Know All Men by These Presents That I, *Harold Beauchamp,* for value received, have bargained, sold, assigned and transferred, and by these presents do bargain, sell, assign and transfer unto _____ 100 shares of the capital stock of the BelmontConstruction Company standing in my name on the books of the said company, and do hereby constitute and appoint _____ my true and lawful attorney, irrevocable, for me and in my name and stead, but to his use, to sell, assign, transfer and set over all or any part of the said stock, and for that purpose to make and execute all necessary acts of assignment and transfer, and one or more persons to substitute with like full power, hereby ratifying and confirming all that my said attorney, or his substitute or substitutes, shall lawfully do by virtue hereof.

In Witness Whereof, I have set my hand and seal hereto the *10th* day of *September, A. D. 1919.*

Sealed and delivered in the presence of

(Signed) Henry W. Crawford

(Signed) Harold Beauchamp. (seal)

$2 In U. S. revenue stamps, cancelled.

Fig. 3

pany to trustees, who have stock certificates made out in their own names as trustees. The trustees then execute to the original owners of the shares "certificates of beneficial interest." In consequence the trustees have the right to vote, and the real owners of the shares have all the other incidents of ownership. In a few states voting trusts have been declared void.

In most states it is held that voting trusts are valid, provided they have a lawful object.

(C) Fraudulent issue of stock by the officers of a corporation.

32. In some states constitutional or statutory provisions exist to the effect that corporate stock shall not be issued except for work or labor done, or money or property received by the corporation. Under such provisions persons to whom is issued stock for which the corporation receives no value are in danger either of having their shares declared void or of being forced to pay the par value of such shares. Where a corporation issues more than the authorized number of its shares of capital stock, a subscriber to such an overissue is not liable on his subscription. And if he has paid money for such spurious shares, he may sue the corporation for reimbursement. If the overissued shares pass into the hands of an innocent transferee for value, the corporation is liable in damages to him for the value of the stock.

ROGERS *v.* GLADIATOR GOLD MINING & MILLING CO., 113 N. W. (S. D.) 86 (1907). The South Dakota Constitution provided that no corporation could lawfully issue stock except for labor done, or money or property actually received. Rogers agreed with the Gladiator Company to help a man named Crabtree in selling the company's stock and in making assays. For these services the corporation agreed to issue certain shares of stock to him. The services having been performed, Rogers sued the Gladiator Company for its failure to deliver the stock. *Held*, the agreement violated the provisions of the State Constitution. Rogers paid the corporation no money or property, and the services performed were rendered to Crabtree individually. Therefore, Rogers could not recover from the corporation.

THE RIGHT OF STOCKHOLDERS AND OTHER MEMBERS OF CORPORATIONS TO A SHARE OF PROFITS

(A) A stockholder's right to dividends.

33. Dividends are profits appropriated by resolution of the board of directors for division among the stockholders. Until dividends are declared, the profits are part of the assets of the corporation, and do not belong to the stockholders individually. Nor is there any debt due from the corporation to them, even though the business is so prosperous that a dividend ought to be declared.

34. The declaration of dividends is largely a matter of discretion on the part of the directors. They will not be interfered with by the courts, unless they act fraudulently or oppressively. Under the laws of most states, even though a corporation has a large surplus fund, if the directors think fit, they may retain it as a surplus instead of distributing it among the stockholders in the shape of dividends.

McNab *v.* McNab & Harlin Mfg. Co., 62 Hun (N. Y.) 18 (1891). McNab was a stockholder in McNab & Harlin Manufacturing Company, which had a capital stock of $150,000 and a surplus of $152,209. Dividends at the rate of 25 per cent. had been paid for a period of ten years. McNab sued to have all or part of the surplus distributed as a dividend. *Held* that as the surplus was profitably employed by the directors in purchasing materials used by the company in its manufactures, and as they considered it for the company's best interests not to divide this surplus, the directors could not be said to have acted unreasonably or capriciously. Therefore, the court refused to interfere.

35. When the directors have lawfully declared a dividend out of profits earned and received, and the time set for paying the dividend arrives, the stockholders become entitled to payment, and there is a debt due them by the corporation. If the corporation withholds payment of the dividend after it is due, the stockholders may sue the corporation for the amount of the dividend.

(B) The rights of preferred stockholders.

36. Preferred stock ordinarily entitles the holders thereof to payment of dividends out of corporate profits before any dividends are distributed among the holders of common stock. Such stock is sometimes called "guaranteed" stock; but this term is inaccurate, as the corporation does not guarantee to pay dividends on it. The rights of preferred stockholders depend upon the contract under which the stock is issued.

37. Preferred stock is of many kinds, varying in accordance with the terms under which it is issued. In some cases the holders are entitled not only to priority in payment of dividends, but also to priority in the distribution of the principal upon the dissolution of the company. In other cases the holders are entitled to priority over the common stockholders merely in the distribution of dividends. These dividends may be cumulative or non-cumulative. Cumulative preferred stock entitles the holders to receive dividends for the years when the company has paid them nothing, before the common stockholders can begin to share in profits. Holders of non-cumulatve preferred stock are entitled only to a preference over the common stockholders in the payment of dividends for the current dividend period (usually a year), without any allowance for the previous periods when the company has paid them nothing.

38. Dividends on either preferred or common stock must not be paid out of the company's capital stock. Holders of stock of either kind are members of a corporation, and not its creditors, at least so far as respects their shares.

(C) The right to a dividend as between various claimants.

39. Usually the person in whose name stock stands when the dividends are payable is entitled thereto. If a stock certificate has been delivered to a purchaser prior to the declaration of a dividend, but the shares represented by it have not been transferred to the purchaser's name, the company pays the dividend to the registered owner, who is bound to turn it over

to the purchaser, the real owner. Sometimes when a dividend is declared payable at a later date, stock changes hands between the day of declaration and the day when the dividend is payable. In the absence of any custom or agreement to the contrary, the owner of the stock at the time of the declaration is entitled to it, although it may not be payable until after the sale.

40. Where stock has been pledged but not transferred to the pledgee's name, the pledgor being the registered owner, the corporation will pay dividends to him. If the pledgee has had the stock transferred to his own name, the corporation will pay the dividends to him, but he must account to the pledgor for them.

(D) A stockholder's right to subscribe for new stock.

41. When the stock of a corporation is to be increased a stockholder is entitled to preference in subscribing for new stock, unless a statute or other local law provides otherwise. He may demand such a proportion of the new stock as the number of shares already owned by him bears to the whole number of shares in existence before the increase.

Jones *v.* Morrison, 31 Minn. 140 (1883). Jones, Dorilus Morrison and Clinton Morrison were stockholders and directors in the Minneapolis Harvester Works. While Jones by reason of ill health was absent in Europe, the Morrisons, being majority stockholders, caused a stockholders' meeting to be held on January 3, 1882, at which it was resolved to issue 7,000 shares of new stock and give the existing stockholders the right to subscribe for it before January 24. At a subsequent meeting of the board of directors, also controlled by the Morrisons, it was resolved that as none of the new stock had been subscribed, the entire issue should be sold to the Morrisons and their friends, which accordingly was done. Notices of these meetings were sent to Jones, but he was in a part of Europe from which he could not have forwarded his subscription within less than eighteen days. As soon as Jones learned of these proceedings, he sued to have them set aside. *Held* that Jones was entitled to an opportunity to subscribe for and take new stock in proportion to the old stock held by him. The Morrisons had known of his absence abroad, and apparently had sought to take unfair advantage of it.

THE RIGHTS OF STOCKHOLDERS AND OTHER MEMBERS OF CORPORATIONS TO CONTROL AND INSPECT CORPORATE AFFAIRS

(A) The right of a member to vote at corporate meetings.

42. A stockholder has the right to vote at corporate meetings. The holder of the legal title to shares is the one who may vote them. The stock certificate and the transfer books are good, but not always conclusive, evidence as to who has the legal title. In disputed cases, the judges of election determine who is entitled to vote.

43. When nothing appears to the contrary in the laws of the state or the charter of the corporation, each stockholder is entitled to one vote for each share of stock he owns. The statutes of some states, in order to give the minority stockholders representation on the board of directors, confer the right of cumulative voting. If cumulative voting is allowed at elections of directors, each stockholder is entitled to as many votes as shall be equal to the number of his shares of stock multiplied by the number of directors to be elected. He may cast them all for a single director or distribute them among two or more, as he sees fit.

1. Joint Owners

44. Where several persons own stock jointly, either in their own right or as fiduciaries, ordinarily the stock cannot be voted unless all agree upon the way the vote shall be cast. But in some states a majority is allowed by statute to vote stock held jointly.

2. Voting by Fiduciaries

45. Where one holds stock as a trustee, executor, or administrator, he is entitled to vote thereon.

3. Voting by Pledgor

46. In the case of a pledge of stock, the right to vote remains in the pledgor as long as the stock stands in his

name. When the title is transferred on the company's books to the pledgee, he usually acquires the voting power.

4. Voting by Proxy

47. In almost every business corporation the right to vote by proxy is conferred by statute, charter, or by-law. The term proxy usually means a document setting forth the authority granted by a stockholder to his deputy. It is also used to designate the deputy authorized to represent another. The

Know All Men by These Presents:

That I, the undersigned, do hereby constitute and appoint George J. Osborne my true and lawful attorney, with full powers of substitution and revocation, to represent me at the special meeting of stockholders of the Belmont Construction Company, to be held on the 20th day of October, 1921, at 3 o'clock P. M., and do hereby authorize and empower him to vote at the said meeting and at any adjournment thereof, for me and in my name and stead, upon the stock then standing in my name on the books of said company, at any elections then held and on any other matters or questions coming before the said meeting or any adjournment thereof, and I hereby grant my attorney all the powers that I should possess if personally present at the said meeting.

Witness my signature and seal this 1st day of October, 1921.

[*Signed*] Arthur Sedley (L. S.)

In the presence of
[*Signed*] Henry P. Thornton

10 cents in U. S. revenue stamps, cancelled.

Fig. 4

document itself need not be acknowledged before a notary, but should be duly executed and witnessed. In Fig. 4 is shown a form of proxy in general use.

(B) The manner of conducting meetings of corporate members.

48. As a general rule, all meetings of stockholders should be held in the state where the corporation was chartered. But when a corporation is chartered by several states, a stockholders' meeting held in one of these states is valid with respect to the property in all of them. The stockholders do

not have to hold a meeting in each of the states in which the corporation is domiciled. The laws of some states authorize corporations formed thereunder to hold meetings anywhere.

49. Notice of any special meeting should be given to every stockholder of record. Notice of the annual or stated meetings is not always necessary, if the date upon which they shall be held is specified in the by-laws. Stockholders are presumed to be familiar with these provisions, but it is always wise to give them formal notice. The length of notice required is generally stated in the statute law or in the particular company's by-laws, and varies from two to sixty days or more. Where the statutes and the by-laws are silent on the subject, a reasonable notice is required.

50. When a meeting has regularly convened, the first thing to determine is whether or not a quorum is present. Usually the local statutes, or the charter or the by-laws, provide how many shares of stock must be represented in person or by proxy to constitute a quorum. In the absence of such provision a majority of the whole number of shares is sufficient.

51. The meeting is usually called to order by the president or some other duly authorized officer. When no presiding officer is designated by the charter or the by-laws, the stockholders should proceed to elect a chairman. Some one should also be chosen to take the minutes of the meeting.

(C) The business transacted at meetings of corporate members.

52. Stockholders' meetings are held for the purpose of having collective action by the stockholders, in order to register the corporate will. As individuals, the stockholders cannot agree to increase the capital stock or to merge with another corporation, or to make other fundamental changes in their organization. For these purposes corporate assent, duly obtained at a stockholders' meeting, is requisite.

53. At a general or stated meeting of the stockholders any legitimate corporate business may be transacted, subject,

however, to any requirement as to prior notice of proposed amendments to the charter or the by-laws or other important matters. At a special meeting, the only business proper to be transacted is that for which the meeting has been called.

(D) The right of a member to inspect the company's books, and to interfere in the management of its affairs.

54. Usually a stockholder has a limited right to inspect the books of the corporation at a reasonable time and place, and for a proper purpose. Thus, ordinarily he may inspect the list of stockholders, with a view to canvassing for an approaching election of directors. If he has good reason to suspect fraud on the part of the management, generally he may examine the company's books in order to learn the facts and take proper legal action. The right of inspection includes the right to make copies of the books and records of the company. The corporation may make reasonable regulations governing the manner in which this right shall be exercised, but ordinarily cannot deny it altogether in cases where a stockholder's best interests seem to require an investigation. If the corporation wrongfully refuses to permit a stockholder to examine the books, he may get an order of court to enforce his demands.

55. The principle of majority rule obtains in the management of corporations, and a minority stockholder merely as such has little voice in the control of his company's affairs. But a minority stockholder is entitled to relief where the corporation exceeds its powers or otherwise acts illegally or fraudulently.

Bixler *v.* Summerfield, 195 Ill. 147 (1902). The Story Finishing Company had a capital stock of 300 shares of the par value of $50 each. Bixler owned 58 shares, Summerfield 241 shares, and Hoff 1 share. Bixler charged that Summerfield was voting away the corporate profits for salaries for himself and family. Summerfield was getting a salary of $35 a week, his wife $25 a week for work formerly done for $3.50, and his sister $3 a week for signing her name as secretary to a few letters of notification to stockholders. Moreover, he had reduced Bixler's salary from $15 to $12 a week. Bixler sued Summerfield and Hoff, the

majority stockholders, to prevent them from continuing to vote excessive salaries. *Held,* Bixler was entitled to relief. It was clear that the majority stockholders had acted in bad faith.

THE LIABILITIES OF STOCKHOLDERS

(A) Liability on stock subscriptions.

56. The relation between a corporation and its stockholders is contractual. The contract of subscription fixes the rights and the obligations of both parties. The provisions of the statute under which the corporation is formed, whether it is the general incorporation act or a special act of the legislature, are parts of the contract. When a person signs his name to the contract of subscription or articles of incorporation, and agrees to take the number of shares set opposite his name, he is liable for the face value of the stock.

57. The chief incident of corporate membership is limited liability. Ordinarily, membership in a corporation does not entail any liability except for the amount subscribed. In most cases the liability of stockholders is limited to the par value of the stock for which they have subscribed. In some states a greater liability is imposed by statute. Under the banking laws of the United States, stockholders in national banks are liable for double the par value of their stock.

58. Payment for shares of stock need not be in money, but must be "in money or money's worth." Where payment is made in anything else than money, as, for instance, services or patent rights, the payment will be held to be valid only where it is made in good faith, and where an honest valuation is placed on the services or the patent rights.

(B) Liability of original subscribers and other stockholders to pay assessments.

59. As a rule, original subscribers to the capital stock of a corporation are bound to pay the face value of the shares. Where a subscription to stock is not payable either at once or at some definite time in the future, the directors may make

a demand upon the stockholders for payment of all or part of the unpaid balance by a certain date. This is termed "making a call."

60. Notice of a call ought always to be given to the stockholders. If notice has been duly given, upon the expiration of the prescribed period, interest may be charged against any delinquent stockholder.

61. For a sufficient consideration the corporation may discharge a stockholder from his obligation, provided the rights of creditors are not prejudiced thereby. Unless the obligation is discharged, the corporation, if calls are not paid when due, may: (1) sue the delinquent holder for the amount of the assessment; or (2) sell his shares to raise what he owes. If the latter course is taken, and the proceeds of the sale are insufficient to pay the amount of the assessment, the corporation still has the right to sue the stockholder for the deficit.

62. The registered owner of stock is generally liable to pay assessments. Where the owner of stock which is not fully paid up transfers it, and the transfer is duly recorded in the company's books, he is not usually liable for subsequent calls in the absence of a charter or statutory provision, or an express agreement, fastening such liability on him.

(C) Liability of stockholders for certain corporate debts.

63. In certain states, a liability for more than the par value of the stock subscribed is imposed by statute. In California and Minnesota, except in the case of corporations carrying on exclusively a manufacturing, mining, or mechanical business, double liability is imposed by statute. Stockholders of certain New York corporations are liable for corporate debts in full.

64. In Indiana, Massachusetts, Michigan, New York, North Dakota, Oklahoma, Pennsylvania, South Dakota, Tennessee, and Wisconsin, the stockholders of certain corporations are liable for wages due employes. To enforce this

liability, demand must be made within a specified time. The statutes of many states provide that if any part of the capital stock is refunded to stockholders before the payment of all corporate debts for which such refunded capital stock would have been liable, the stockholders become individually liable to creditors of the corporation for the amounts respectively returned to them. In a few states stockholders are personally liable for all debts of the corporation unless this liability is expressly limited by the charter.

THE DIRECTORS

(A) The qualifications of directors.

65. Business corporations are usually managed by a board of directors, a president, one or more vice-presidents, a secretary, a treasurer, and such other officers and agents as the corporation may appoint. Usually directors of business corporations may act also as officers, and are entitled to receive such compensation for their official services as the by-laws or the board of directors may determine.

66. In the absence of statutory provision or by-law regulation, no particular qualifications are required of directors. The laws of many states require at least one of the directors of a corporation chartered thereunder to be a resident of the State from which the charter was obtained. Foreigners, married women, and even minors, are found on the boards of various corporations.

67. The laws of some states provide that each director of a company chartered thereunder must own at least one share of the company's stock. And even though the laws of a state which charters a concern are silent on this point, the company's by-laws may require that each director shall own at least a certain number of shares.

(B) The powers of directors.

68. The directors are the managers of the company. Generally speaking, whatever the corporation can do, can, in the

absence of a provision to the contrary, be done by the board of directors acting in their collective capacity. Ordinarily, they may issue corporate stock and make contracts concerning it; make assessments upon stock which is not paid up; declare dividends; prosecute and settle lawsuits; appoint the president and other officers; mortgage the company's property, and generally direct its affairs.

69. When the number of directors is reduced below a quorum, their power is suspended. In the absence of a provision to the contrary, a majority of the whole number of directors is necessary to constitute a quorum for the transaction of business. Unlike stockholders, directors cannot vote by proxy; therefore, a director who is present only by proxy cannot be counted in making up a quorum. Where the regulations of the company do not prescribe a place of meeting, the choice of locality is within the discretion of the directors. But the directors of Louisiana corporations must hold their meetings in that state.

70. In case of vacancies in the board of directors caused by death, resignation, or removal, usually the remaining directors are empowered, by statute or by-law, to supply the vacancies thus created until the next election. If they fail to do so, the fact that there are vacancies does not impair the validity of their acts at meetings where there is a quorum. If the directors are not authorized to fill vacancies, sometimes a special meeting of the stockholders is called for this purpose.

Sylvania & Girard R. R. Co. *v.* Hoge, 59 S. E. (Ga.) 806 (1907). The Georgia Code provided that railroads should have not less than five directors. By reason of the death of one of its members, the board of directors of the Sylvania Railroad Company was reduced to four. Hoge and other stockholders sued the railroad company and its directors to cause a meeting of the stockholders to be held for the purpose of electing directors, the time for the annual meeting at which directors should have been elected having passed. *Held* that the directors should be ordered to cause a stockholders' meeting to be held. In the absence of any statute or by-law authorizing directors to supply a vacancy in their board, usually nobody but the stockholders can exercise this power.

71. Generally the by-laws authorize the delegation of certain powers of the board of directors to committees. A com-

mittee may consist of a single member. Only the powers that have been delegated to them can be exercised by such committees.

COMMERCIAL WOOD AND CEMENT CO. *v.* NORTHAMPTON PORTLAND CEMENT CO., 82 N. E. (N. Y.) 730 (1907). The directors of the Northampton Portland Cement Company delegated to an executive committee certain power, subject at all times to the orders of the board. At a meeting of the executive committee an agreement was made with the Commercial Wood and Cement Company to appoint the latter concern the Northampton Company's sole selling agent for a period of five years, although a meeting of the Northampton Company's directors had been called for the afternoon of the same day. The secretary of the Northampton Company promptly notified the Commercial Company that the agreement was under consideration by the Northampton Company's board, and two hours after it had been entered into by the executive committee it was rejected by the board. The Commercial Company thereupon sued the Northampton Company for damages for breach of contract. *Held* that the executive committee had no authority to make such contract. The call for a directors' meeting had suspended the authority of the executive committee. Moreover, the contract being an unusual and extraordinary one, the executive committee was not authorized to make it.

72. Full and accurate minutes of all meetings should be taken. The minutes should be signed at the end by the one who acted as secretary of the meeting. In some states the law requires that in certain corporate proceedings minutes of the transactions be taken and preserved, and provides that otherwise the proceedings will be invalid.

(C) The compensation of directors.

73. A director of a corporation is not entitled to pay for his services without an express contract or some provision in the charter or the by-laws to that effect. As a matter of fact, directors are rarely compensated for their services commensurately with the ability required and the responsibility involved. In the case of many corporations an honorarium of $5, $10, or $20 is allowed for attendance at each board or committee meeting.

(D) The obligations and liabilities of directors.

74. As directors are the unpaid representatives of the corporate members, usually they are responsible only for dis-

honesty, breach of trust, or gross negligence. When directors act faithfully, keep within the powers given them, and follow the statutes and by-laws, they are not liable for any loss which may occur. They do not insure the success of any action undertaken by the company.

CASE *v.* DELANO, 121 Ill. 247 (1887). Case, a depositor in a bank, sued Delano and the other directors for negligence in permitting the bank to be held out as solvent, when, in fact, it was at the time insolvent. *Held* that Case was entitled to recover. Directors are bound to observe care and diligence and are liable for injuries resulting from their gross negligence. Delano and the other directors had been quite neglectful of their duties, and Case, therefore, had the right to hold them for the damages he had sustained.

75. The position of director of a corporation is a fiduciary one, and therefore the ordinary rules applicable to any fiduciary apply. Ordinarily a director cannot represent the corporation in dealings wherein he has a conflicting personal interest.

76. If the directors of a company declare a dividend when they know that there are no profits or surplus on hand with which to pay it, so that upon payment the capital stock is impaired, the directors are liable to creditors of the corporation for the amount of the dividend so paid.

THE PRESIDENT AND THE OTHER OFFICERS

77. The by-laws of the company and the resolutions of the board of directors ordinarily regulate the duties, the powers, and the compensation of corporate officers. Usually officers have only such powers as are thus conferred upon them. As they are not the general agents of the company, they can bind it merely in so far as they are authorized. Express authority is not in all cases necessary. Authority may be implied from the previous business dealings of the corporation. Where officers assume to do certain acts, and the corporation in the past has repeatedly ratified the performance of similar acts by them, generally they will be held to have the necessary authority.

(A) The president.

78. The chief executive officer in most corporations is the president. He generally assumes the supervision of corporate affairs, and sees that the orders of the directors are carried out. The presidents of most companies are either expressly granted extensive powers, or allowed to exercise such powers by general acquiescence. But otherwise, a president's powers are quite narrow.

79. If the president or any other representative of a company exceeds the authority which has been granted to him, the corporation should promptly repudiate his action. It must, when the unauthorized action is disaffirmed, return any benefits which it has received under such action. It cannot repudiate a contract and retain the benefits received thereunder.

(B) The secretary.

80. The secretary is generally the clerk of the corporation and the custodian of its records. He should take minutes of the meetings of the directors and of the stockholders, and in certain cases, of committees. These minutes should be carefully preserved. He is also usually charged with the safekeeping of the corporate seal. He has power to affix the corporate seal to papers authorized to be executed on behalf of the company, and to attest the seal when duly affixed.

(C) The treasurer.

81. The treasurer is usually the custodian of the funds and securities belonging to the corporation. In most companies the treasurer takes charge of, or supervises, the books of account. He should be careful as to the bank or trust company in which corporate funds are deposited. In order to be protected, he should have the depository designated by the board of directors.

THE MERGER AND CONSOLIDATION OF CORPORATIONS

82. The merger and consolidation of corporations may be effected in various ways. The merger of corporations, strictly speaking, is the combination of the respective rights, interests, and franchises of two or more corporations by legal agreement of the stockholders, acting under statutory authority. A combination, which usually does not amount to a technical merger, may be effected through one corporation's purchasing or leasing all the assets of another, or through the acquisition of control by one corporation of another's stock.

83. Statutory authority is always necessary to effect a real corporate consolidation. In most states legislative sanction is given to the consolidation of nearly every kind of corporations. For example, generally non-competing railroad companies may consolidate.

84. Some of the statutes which authorize consolidation provide that the consent of two-thirds or of three-fourths of the stockholders must be obtained. In many states statutory provision is made for the purchase by the corporation of the stock of dissenting shareholders.

85. To effect a valid consolidation, the statute must be strictly followed. The usual procedure is as follows: (1) an agreement as to terms by the directors of the consolidating corporations; (2) submission of the directors' agreement to the stockholders of each company at a duly assembled meeting; (3) assent of the stockholders to the directors' agreement by the required vote; (4) filing of certified copies of the agreement, and favorable election return, in the same offices in which the original certificate of each of the consolidating corporations was filed.

86. The effect of consolidation under statutory authority is usually to dissolve the old corporations, the merger whereof creates a new corporation. This new corporation succeeds to all rights and obligations of constituent companies.

87. When a combination is effected by the sale or the lease of all the assets of one corporation to another, sometimes the latter company issues its own stock or bonds to the stockholders of the old company, who thereby become stockholders or bondholders in the purchasing or leasing corporation. A public utilities corporation can seldom sell out all its property in this manner. But statutes very generally permit public utilities companies, such as railroad corporations, to lease their property to another company, provided such action is authorized by a majority of the stockholders.

88. Another method of consolidation is by uniting in the hands of an individual, a syndicate, or a holding corporation a controlling interest in several companies. This may be done through companies chartered in Delaware, Maine, New York, or one of the many other states under whose laws corporations are authorized to hold stock in other corporations.

89. Over thirty states have limited the combination of corporations by means of anti-trust laws. A "trust" is a combination of corporations or individuals, or both, for the purpose of controlling production with a view to repressing competition and raising prices. Even under the old rules of the common law, most agreements and monopolies in restraint of trade were against public policy, and, therefore, unlawful and void. The Federal Congress has attempted to prevent illegal combinations so far as respects interstate and foreign commerce by passing the Sherman Act of July 2, 1890, and the Clayton Anti-Trust Act and the Federal Trade Commission Act, both in 1914. Some legislatures are beginning to realize that they have impaired the country's prosperity by their incessant attacks upon corporations, and that it is in many cases desirable to permit the consolidation of companies. The advantages to be gained from doing business on a large scale are obvious, and it is only the occasional abuses of great combinations of capital that should be repressed.

BONUS AND TAX LAWS—REGULATION OF DOMESTIC AND FOREIGN CORPORATIONS

(A) Bonus and tax laws.

90. A state may tax a corporation just as it may tax natural persons. Generally speaking, there are three kinds of corporate property which may be taxed: (1) corporation franchises; (2) property held by a corporation, such as lands and money; (3) capital stock in the corporation, either held by the corporation itself or by individual stockholders.

91. The power of a state to tax a corporation is limited to matters which do not come under the exclusive control of the Federal Government. For example, a state may not impose a tax upon a railroad company which will amount to a regulation of foreign or interstate commerce.

92. In the absence of constitutional or statutory prohibition, the proper state authorities may exempt a corporation from taxation. But such exemption must be clear and unequivocal.

93. Usually two kinds of franchise charges are imposed by a state: (1) the bonus or organization fee, payable when a company is formed; (2) the franchise tax on corporations payable annually.

94. An organization fee is the amount of money paid to a state for the privilege of becoming a corporation. A franchise tax is the amount of money paid annually to the state for the privilege of doing business as a corporation.

95. Nearly all the states exact organization fees before the granting of a charter. Moreover, many states impose an annual franchise tax upon the total amount of outstanding capital stock. In some of these states, however, certain manufacturing and other companies are exempted from the payment of annual franchise taxes.

(B) Reports required of corporations.

96. In almost every state corporations chartered or doing business therein are required to file annual reports in a designated state office, setting forth the condition of such corporations. The matters about which information must be given vary in different states. The following information is required in some states: (1) names and addresses of officers and directors; (2) amount of capital stock authorized and paid in; (3) amount of bonded or other indebtedness; (4) value of real and personal property; (5) name of each stockholder, and number of shares held by him; (6) location of principal office within the state, and name of person in charge thereof.

(C) Registration by foreign corporations.

97. The term "foreign corporations" embraces not only corporations chartered by another nation, but also those chartered by another state of the Union. The various states have passed acts prescribing the terms and conditions upon which foreign corporations may enter and do business. These acts do not differ very greatly. Most of them direct that a foreign corporation shall appoint an agent residing within the state, upon whom legal process against the corporation may be served, and shall designate its local business office. In some states a specified state official must be appointed as the foreign corporation's local representative for the purpose of accepting service of process against the corporation. Some states require also that a certified copy of the charter must be filed in a certain state office, as well as in a local office in the county where the company's principal place of business is to be located.

98. A corporation has no right to enter and do business in a state other than that in which it was chartered. The recognition of foreign corporations in this respect is a matter largely dependent upon state comity. Therefore, the state may exclude foreign corporations altogether, or impose any conditions upon them before they shall have the right to do business. These conditions must, of course, not be repugnant

to the Constitution of the United States. Thus, the right of a state over foreign corporations does not extend to those engaged in interstate commerce which merely send goods through or into the state.

99. Sometimes it is difficult to determine whether or not a foreign corporation has entered into a state and transacted business there. For example, a corporation chartered in one state may sell goods in another state by means of correspondence or a non-resident traveling salesman, without transacting business in the foreign state within the legal meaning of the words "transacting business." Neither, under the law of most states, does the making of a single contract within a foreign state constitute the "transaction of business" therein. So also it has been held by some courts that a corporation may rent an office in a foreign state, and put a selling agent in charge thereof, to distribute samples among its customers without "doing business" in the foreign state.

100. Various penalties are imposed in different jurisdictions upon foreign corporations which do business without first complying with the provisions of the local statute. In some states the right of a corporation to sue in the courts of the foreign state is withheld until the statute is complied with. In others foreign corporations which have not complied with the local statutes are absolutely forbidden to sue on contracts made before they have obtained a permit to do business. Some other states declare that contracts made by foreign corporations before complying with the local statutes are absolutely void. In other states fines are imposed or the state officials are authorized to oust the foreign corporation.

PUBLIC AND SEMIPUBLIC CORPORATIONS

101. Corporations are either public or private. Public corporations are created by the government for public purposes. Most private corporations are organized by private individuals. Moreover, there are certain loosely organized governmental districts, not really corporations, which are called

quasi corporations. *Quasi,* a Latin word, means "as if." It is used to denote that two things are similar to each other, but not sufficiently alike to be identical.

(A) Quasi corporations.

102. *Quasi* corporations are political or civil divisions of the state, created by statute without the consent of the inhabitants thereof, and invested with particular powers to aid in the administration of the government. These include most counties, townships, school districts, and road districts, as well as many boards of commissioners, supervisors, or school trustees: in short, most local divisions of the state government other than municipalities. They differ from municipal corporations in that they are involuntary organizations, having no charters, and existing exclusively for purposes of civil government.

103. The most familiar type of *quasi* corporation is the local division known as a county. The towns of the New England states, and the townships of some of the Eastern and Southern states resemble counties in many particulars.

104. The government of a county is intrusted to an official body, which may be a board of supervisors or commissioners chosen by the people. The county government has only such powers as are expressly conferred upon it by the statute establishing it as a territorial division for purposes of civil government, or necessarily implied therefrom. Ordinarily, it may exercise the power of eminent domain, by taking private property for public use, without the owner's consent, upon making compensation therefor. It may also purchase, hold, and sell real estate, provide for the support of the poor and the maintenance of public schools, contract for the erection and furnishing of public buildings, and generally do any other acts which are necessary and proper for the accomplishment of the objects for which it was created.

105. As the power to borrow money is not implied in the case of most *quasi* corporations, one should not make a loan thereto unless all the proper legal steps have been taken. For

example, in order that a county may be bound by contract for any indebtedness, the following conditions must be fulfilled: (1) the county must be authorized by statute to enter into such a contract; (2) if the consent of the people is required, it must be obtained in the manner prescribed by law; (3) the county officers must execute the contract in the manner prescribed by law.

(B) Municipal and other public corporations.

106. A municipal corporation is a public corporation created by the legislature for purposes of government, and invested with certain powers of legislation to effectuate the objects for which it was established. Cities are the most common examples of municipal corporations. The governments of the United States and of the several states of the Union are not municipal corporations. They are self-existing bodies formed of a multitude of persons united by common interest and by common laws. They derive their powers largely from the consent of the people who compose them. Municipal corporations may be created: (1) by the United States Congress; (2) by the state legislatures; (3) by the territorial legislatures when so authorized by Congress. Upon the creation of a municipality, usually a document called the municipal charter is issued to it. Ordinarily this defines the rights, privileges, and powers of the corporation and establishes its form of government.

107. Unlike the charters of private corporations, municipal charters are not contracts between the state and the corporation or incorporators. Therefore, unless prohibited by the state constitution, the legislature may increase or decrease the territory of a municipal corporation without the consent of its members, divide the corporation into two or more, or combine two or more corporations into one, amend the charter so as to increase or diminish municipal powers, and even repeal the charter so as to dissolve the corporation.

108. The powers of municipal corporations are of two kinds: (1) public; (2) private. The former are those relating to the governmental powers of a municipality, to which, as a

division or agency of the state, are granted certain sovereign powers. These usually include the powers of eminent domain, of promoting public education, of police, and certain other powers exercised by the municipality for the welfare of the community, but for which it receives no consideration. The private powers exercised by a municipality may be roughly grouped together as those from which it derives an income. These usually include, among others, the power to erect and maintain gas, water, and electrical plants, and other works of public utility.

109. While municipalities constitute the majority of all public corporations, there are other corporations of this kind. Thus, if a school district is granted a charter, it is a public corporation, although not a municipality.

(C) Semipublic corporations.

110. Semipublic corporations are private corporations performing public functions, supplying public utilities, or operating under municipal franchises. These include the following: bridge, canal, and ferry companies; electric light and power companies; gas, water, and sewer companies; railroad, street railway, turnpike, and navigation companies; telegraph and telephone companies; pipe-line, grain elevator, and irrigation companies, and many others. Semipublic corporations, being created primarily for the private profit of their members, are essentially private corporations. They have all the powers and incidents of other private corporations, and are owned by their stockholders and managed by their directors and officers in much the same way.

111. Many semipublic corporations, such as railroad companies, are given the right of eminent domain. See Art. **104.** Many of them, such as street railway companies, use the public highways. In view of such special privileges, and of the fact that they are formed to earn a profit by serving the general public, they are subject in a high degree to public regulation and control, in order that the public interests may be protected. For example, the legislature, directly or through a Public Ser-

vice Commission, may compel semipublic corporations so to conduct their business as not to impose unreasonably high charges on the public, or unnecessarily to expose it to harm or danger.

WILCOX *v.* CONSOLIDATED GAS CO., 212 U. S. 19 (1909). The New York State Legislature by a law passed in 1906 limited the price to be charged for gas to 80 cents per 1,000 cubic feet. The Consolidated Gas Company asked that the Public Service Commission be restrained from carrying out this law. *Held* that the law was reasonable. Public service corporations, such as gas companies, are subject to the legislative right to fix rates which permit not more than a fair return on the property used. Six per cent. is a fair return on the value of property employed in supplying gas in the City of New York, and a rate yielding that return is not confiscatory. In the absence of proof that the 80-cent-gas law would yield the Consolidated Gas Company a return of less than six per cent. on its investment, the Public Service Commission would not be restrained from enforcing the law.

THE TERMINATION OF CORPORATIONS

112. The termination of agency and of partnerships has been treated under five subdivisions, which will be followed in considering the termination of corporations. The dissolution of a corporation may be caused: *first,* by agreement; *second,* by performance; *third,* by breach; *fourth,* by impossibility; *fifth,* by bankruptcy or insolvency.

(A) Termination of corporations by agreement.

113. The dissolution of a corporation may be effected by the voluntary surrender of the powers and franchises granted in the corporate charter, if the surrender is accepted by the state. But in the case of strictly private corporations, which have no public duties to perform, the consent of the state is not necessary. The state cannot compel a private corporation to remain in existence, and such a corporation may dissolve itself by the consent of its members.

114. In most business corporations the unanimous consent of all the stockholders is not necessary to a surrender of its privileges. Usually the majority of the stockholders, in the

exercise of a sound discretion, may decide to wind up the business even against the will of the minority.

115. The statutes of nearly every state provide what steps shall be followed in winding up a corporation by agreement. In order to be secure, the provisions set forth in the statute should be strictly followed.

(B) Termination of corporations by performance.

116. Where a corporation has been expressly chartered merely to put through a certain piece of work, its activity will be terminated on the performance of that work. Or, if a certain period has been fixed for the corporate existence by its charter or a local statute, it will come to an end at the expiration of that period, unless its franchises are renewed. In most states provisions are made for continuing, under certain conditions, the existence of corporations whose charters are about to expire.

(C) Termination of corporations by breach.

117. The termination of a corporation may be effected by an abuse of the powers granted to it, or by the failure to exercise them. Either of these causes is a ground for a proceeding by the state to have the corporate charter forfeited.

People *v.* North River Sugar Refining Co., 121 N. Y. 582 (1890). The North River Sugar Refining Company agreed with certain other refiners of sugar to select a board of trustees, and to turn over to this board the stock certificates representing the ownership of all the companies. The refineries were to be managed and operated by the board for the common benefit. Profits and losses were to be shared in certain proportions. *Held*, this was a consolidation for the purpose of creating a "trust" unlawful and injurious to the public interest. It was, therefore, ground for an action by the attorney-general in the name of the state to have the corporation dissolved and its charter forfeited. See Art. **89**.

(D) Termination of corporations by impossibility.

118. The dissolution of a business corporation is seldom effected by impossibility. Even if all the stockholders in a business corporation were to die at the same time, their shares would pass automatically to their executors or administrators, and the corporate existence would be uninterrupted. But if a

statute is passed which makes it unlawful for the corporation to continue doing the business for which it was chartered, there is usually nothing left but to dissolve the company.

(E) Termination of corporations by bankruptcy or insolvency.

119. Neither insolvency nor the appointment of a receiver necessarily brings about the dissolution of a corporation. But these things generally lead in the end to its dissolution. See under Discharge of Contracts by Bankruptcy, Art. **32** and following.

120. In many cases when a corporation has become involved in litigation as a result of financial difficulties, and there is danger that the corporate property may be lost or misapplied, receivership proceedings are instituted. A receiver is a person appointed by a court to take charge of and administer the corporate property under the court's direction for the benefit of the creditors, stockholders, and other persons who are ultimately entitled thereto. Receivers are officers of the court and must account to it.

121. The courts usually have power to appoint receivers when, in the exercise of their discretion, they deem such appointment necessary. This power may be exercised in the following emergencies: (1) in case of insolvency; (2) in case of mismanagement and misapplication of the corporate funds by the officers or directors; (3) in case creditors have been unable to satisfy their claims by means of the ordinary legal process and apply to the local court for assistance.

122. The appointment of a receiver usually has the effect of making it impossible for the corporation to exercise certain corporate powers, because as a rule the decree appointing a receiver gives him custody and control of the property belonging to the corporation. But ordinarily any corporate powers which are not conferred upon the receiver may still be exercised by the corporation. When the receivership is terminated, ordinarily the company may resume the powers which it had prior to the appointment of the receiver.

123. In many of the states the powers of receivers are fixed by statute. Where the local statutes do not define their powers, they have only such as the court may confer upon them. Generally a receiver succeeds to all the rights that the corporation had before his appointment. So also usually any defenses to claims which were good against the corporation before he was appointed may be set up against an action brought by him as receiver, to enforce such corporate claims.

AMERICAN BUSINESS LAW
(PART 7)

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PERSONAL AND REAL PROPERTY

THE VARIOUS KINDS OF PROPERTY AND THE ACQUISITION AND TRANSFER THEREOF

1. Property is the right which one man has to hold and dispose of certain real or personal estate as he may see fit, to the exclusion of all other persons. The word "property" is derived from the Latin word *proprius,* meaning "one's own." All things are not the subject of property. A person cannot appropriate the sea or the air so as to acquire an exclusive right of property in either of them.

2. Property is of two kinds, real and personal. Real property or real estate is usually permanent, fixed, and immovable. To this class belong land, structures thereon, fixtures thereto, and rights issuing out of, annexed to, or exercisable within land. Personal property, which consists for the most part of goods and chattels, is usually movable, so that it may be carried about by the owner from place to place. Books, merchandise, mortgages, and bank notes are familiar kinds of personal property.

3. In this part we shall consider contracts affecting property and the various kinds of property rights. These rights may be obtained in two ways: (1) by original acquisition; (2) by transfer.

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(A) Original acquisition of property.

4. We shall treat of the original acquisition of property as made: (1) by occupancy; (2) by accession; (3) by intellectual labor.

1. By Occupancy

5. The title to most lands is derived from our national, state, or colonial governments, and the question of title by occupancy merely is unimportant. But the continuous, exclusive, notorious, and unopposed occupancy of another's land in hostility to his rights will finally give the occupant title. Usually the period of twenty or twenty-one years outlaws the true owner's claim.

Overfield *v.* Christie, 7 S. & R. (Pa.) 173 (1821). In 1788 Nathan Abbott settled on certain ground, which he improved and sold to Lazarus Ellis, who afterwards sold it to Peter Osterhout. After Osterhout's death, his widow and son were sued by Overfield, who claimed under a grant from the State of Pennsylvania in 1784. *Held*, even though Abbott was originally a trespasser, the exclusive and notorious possession maintained by him and his successors for over twenty-one years, in hostility to the real owner's rights, ripened into title. The various periods, during which Abbott and his successors had occupied the land, could be added together in order to make up the required total of twenty-one years.

6. Formerly goods captured in time of war from an alien public enemy were held to belong to the captor. But now they are held to belong to the nation with whose army the captor is fighting, and he has only such interest in them as that nation's laws prescribe.

7. If the owner of personal property loses it, the finder is entitled to it as against every one but the owner. The finder's title will become perfect if he is unable to discover the owner. But the finder of a lost article is not entitled to a reward from the owner for returning it if none has been promised. Neither has he a lien on the property for the value of his services in keeping it. He must deliver it to the owner on demand.

8. If the owner of personal property abandons it, showing clearly his intention to relinquish his ownership, the finder thereof will have a perfect title.

2. By Accession

9. Accession is defined as the right to all that one's property produces. This includes the crops yielded by land and the increase of animals. Under this head we should also mention the increase of real estate by the addition of portions of soil gradually washed up by the sea or deposited through the operation of other natural causes. The deposit itself is called alluvion. The act by which the deposit is added to the soil is called accretion, which comes from the Latin verb *accrescere,* to grow to. Generally the owners of lands touching on water acquire by virtue of their riparian rights any gradual accretions to the land brought about by the operation of natural causes.

3. By Intellectual Labor

10. By statute the right to the exclusive use for a limited time of their original works and inventions is secured to authors, composers, and inventors. A patent is a grant by the National Government of the exclusive privilege of making, using, and selling an invention, and of authorizing others to make, use, and sell it for 17 years. A copyright is a grant by the National Government to authors of literary or artistic productions of the exclusive privilege of printing, publishing, and selling, and authorizing others to print, publish, and sell their productions for a period of 28 years. The acts of Congress also protect the holder of a copyrighted dramatic or musical work from certain unauthorized public performances thereof.

(B) Transfer of property.

11. Title to personal property may be acquired by transfer in two ways: (1) by act of the law; (2) by act of the parties.

1. Transfer by Act of the Law

12. Title derived by act of the law occurs in four different ways: by forfeiture, judgment, bankruptcy, or intestacy.

13. Title by forfeiture is almost obsolete at the present time. Formerly there were numerous ways in which a man

might forfeit his title to property, among which may be mentioned treason, murder, and outlawry. Under the acts of Congress provision is made for forfeiting boats and other conveyances wherein intoxicating liquors have been carried in disobedience to law, or wherein any goods or commodities are deposited, concealed, or removed with intent to defraud the United States of any tax imposed in respect thereof.

14. Title by judgment occurs as a result of a decree entered in a lawsuit whereby one person becomes entitled to take property formerly belonging to another. This may be by means of a judgment by which title to a specific article which was possessed by A is declared to be transferred to B.

15. Title by bankruptcy occurs where by operation of law a bankrupt's property is transferred to representatives appointed to distribute it among his creditors. See Part 4, under Discharge of Contracts by Bankruptcy, Art. **32** and following.

16. Title by intestacy occurs where a person dies without having made a will, and his property is distributed among his relatives in accordance with the intestate law. See Part 10, Arts. **45-54.**

2. Transfer by Act of the Parties

17. The transfer of property by the act of the parties may occur in the following three ways: (1) by a contract of sale or exchange; (2) by means of a gift during the owner's lifetime; (3) by means of a will, which takes effect at the death of the owner of the property affected by it.

18. A sale is a transfer whereby one party passes title to property to another for money paid or promised to be paid. See Part 8, Arts. **1-41.**

19. An exchange or barter is a transfer by which one party passes title to property to another in consideration of the transfer to him of certain other property. See Part 8, Arts. **1-7.**

20. A gift is a transfer of title to property by one person to another without any consideration and out of the giver's bounty.

21. A transfer of title to property by will takes place when a person, usually by means of a written instrument, designates who shall own his entire property or certain parts of it after his death. See Part 10, Arts. **55-68.**

22. In addition to the above mentioned means of acquiring ownership of property, it should be noted that it is possible for a person to acquire a special interest in property without becoming the owner thereof. For example, A may give B the use of A's property for a certain time. In this case, while A has the right of ownership in the property, B has the right of possession. Usually the right of possession of real property is transferred by means of leases. See Part 8, Arts. **45-50.** Usually the right of possession of personal property is transferred by means of bailment contracts. See Arts. **23-41.**

The above mentioned methods of acquiring title to personal property will be discussed under their appropriate heads.

BAILMENTS, INCLUDING CONTRACTS FOR PLEDGING, HIRING, AND TRANSPORTING PERSONAL PROPERTY

THE DEFINITION OF A BAILMENT, AND THE VARIOUS KINDS THEREOF

23. A bailment is defined as a delivery, by one party to another, of personal property which is to be held in accordance with the purpose of the transaction, and is to be returned or otherwise disposed of when that purpose is accomplished. The word "bailment" is derived from the French *bailler,* meaning "to deliver." A bailment involves a delivery of possession of personal property to a person without transfer of ownership to him. The person who transfers the possession of the personal property is called the "bailor," and the person to whom the possession is transferred is called the "bailee."

24. Bailments are of three kinds: (1) for the sole benefit of the bailor; (2) for the sole benefit of the bailee; (3) for the benefit of both bailor and bailee.

25. A bailment for the bailor's sole benefit may occur when A delivers personal property to B who is to take charge of it or is to perform some other service in connection with it merely for A's advantage and without reward.

26. A bailment for the bailee's sole benefit occurs in the ordinary case of a friendly loan of a book, an automobile, or some other article of personal property. Here the bailee has the use of the thing bailed and is to return it to the bailor without giving him any compensation therefor.

27. Under the third head falls the ordinary business bailment, both bailor and bailee deriving reciprocal advantages from the contract. When a man delivers cloth to a tailor to be made up into a suit of clothes, the bailment is one for the benefit of both parties. The bailee is to receive pay for his labor and services, and the bailor is to receive back his property enhanced in value.

28. Bailments for the benefit of both bailor and bailee are exemplified in contracts of pledging and contracts of hiring. A pledge or pawn is a bailment as security for the performace of some undertaking, ordinarily accompanied by a power to sell the thing bailed in case of non-performance. A contract of hiring is a bailment whereby the bailee becomes entitled to the use of the thing, the time, the purpose, and the consideration usually being specified in the contract.

29. When a common carrier undertakes to transport a person's goods from one point to another, the bailment is for the benefit of both parties. This is also the case with warehousemen, commission merchants, factors, and other parties who perform services involving the transportation, custody, forwarding, or sale of other people's goods. Common carriers, being bailees of a special kind to whom particular rules of law apply, are considered separately in Arts. **42-70.**

THE RIGHTS AND THE OBLIGATIONS OF BAILORS, BAILEES, AND THIRD PARTIES

30. In a bailment transaction the bailee is under immediate obligations to the bailor who has delivered the property for a certain purpose. The bailee's obligations to third parties are seldom of great importance. The bailor's obligations are principally to the bailee. His obligations to third persons are of comparatively slight consequence. As a rule, third parties do not figure largely in bailment contracts, which usually contemplate only a relation between the bailor and the bailee respecting the former's property. Ordinarily a bailee is not the bailor's agent, but rather an independent principal, contracting for himself.

(A) The bailee's obligations toward the bailor.

31. The obligations of the bailee toward the bailor depend upon the nature of the bailment. In the case of a bailment for the bailor's sole benefit, the bailee is not liable for failing to undertake the bailment. He is held only to the exercise of a slight degree of care. Once he accepts property as a bailee without hire, he is responsible only for gross negligence in the performance of the bailment.

SMITH *v.* ELIZABETHPORT BANK, 69 N. J. L. 289 (1903). Smith was administrator of the estate of Peter Wyckoff. Wyckoff had delivered three government bonds to the bank for safe-keeping. For this Wyckoff was to be charged nothing. The cashier deposited them in the vault, which was open during business hours. They were stolen by a trusted employe, and Smith sued the bank to recover their value. *Held,* as the bank was a bailee without hire, it was not liable for the value of the bonds in the absence of proof that it was grossly negligent.

SPRINKLE *v.* BRIMM, 144 N. C. 401 (1907). Brimm, as United States Collector, sold three kegs of brandy to Sprinkle. The brandy could not be shipped that day as Brimm had no revenue stamps, but he said that he would get them and promised Sprinkle that, without charge for his services, he would ship the brandy to a party in Kentucky and send Sprinkle the bill of lading. Sprinkle paid for the brandy and the stamps. Brimm put the brandy on a dray which was to go to the railroad station, but did not see that it was properly shipped. Neither did he send Sprinkle the bill of lading. The brandy was never delivered, and Sprinkle sued Brimm to recover the money he had paid. *Held,* Brimm was grossly negligent in not living up to his agreement. Therefore, even

though he was only a bailee without hire, he would have to make good Sprinkle's loss.

32. In the case of a bailment for the sole benefit of the bailee, it is his duty to take extraordinary care of the thing bailed, and he is liable to the bailor for losses resulting even from slight negligence. He must not use the property in any way other than that agreed upon, and must return it when the object of the bailment has been accomplished. Ordinary expenses, incidental to the use of the thing loaned, such as feeding cattle or domestic animals, must be borne by the bailee. He is entitled to reimbursement from the bailor, however, for any extraordinary expenses necessarily incurred in preserving the property.

Ross *v.* Southern Cotton Oil Co., 41 Fed. 152 (1890). Ross lent his barge to the Southern Cotton Oil Company, which used it for a different purpose from that for which it had been lent. While being so used the barge was sunk. Ross sued his bailee to recover for the damage done. *Held* that the oil company was liable. It was merely a bailee without hire, and, having put the barge to another use than that agreed upon, it was liable for any loss or damage, although the barge might have been sunk by some unforeseen chance and without the bailee's negligence.

33. In the case of a bailment for mutual benefit, the bailee is bound to exercise ordinary or reasonable care under the circumstances. He is liable to the bailor for losses occasioned by his neglect of this duty. Failure on the bailee's part to be as careful of the property bailed as he would be of his own property is an indication of negligence. In the case of common carriers, treated further on under The Transportation of Personal Property, a specially heavy liability rests on the bailee.

Hunter *v.* Ricke Brothers, 127 Ia. 108 (1905). Ricke Brothers ran a livery stable. Hunter left his horses with them to be cared for overnight. During the night a fire of unknown origin destroyed the stable and its contents. Hunter sued Ricke Brothers for the value of the horses. *Held*, as this was a bailment for mutual benefit, Ricke Brothers were bound to use ordinary care. In the case of such bailments, upon the destruction of the bailed property generally the bailee must show that it was not due to any lack of care on his part. But here apparently the loss was caused either accidentally or by an incendiary. The bailee's own property was burned along with the bailor's horses, and in order

to recover the bailor must prove that the bailee's want of care helped to cause the loss. As he did not prove this, Hunter could not recover.

34. If the bailee is guilty of any improper use of the bailor's goods, he is liable for the resulting loss. It is his duty to act in good faith. He cannot, therefore, unless authorized by the bailor, sell or pledge the thing bailed or deal with it in any way other than that contemplated by the bailment.

35. The relation of bailor and bailee is one of trust, and the former's rights are usually not extinguished by the passage of time, as in the case of the outlawry of most obligations. Usually in order for him to lose his right to the thing bailed by lapse of time, he must have demanded the return of his property, and, after refusal by the bailee to deliver it, delayed taking action for the statutory period.

(B) The bailee's obligations toward third parties.

36. As respects third persons, a bailee does not incur any special obligation. If, however, he deceives them by pretending that he is the absolute owner, he is liable to them for the consequences of such false pretenses. Ordinarily, the bailee's obligations are owing to his bailor. But if his bailor does not really own the goods, the bailee is liable in case he refuses to deliver them to the true owner upon demand or returns them to his bailor.

Doty *v.* Hawkins, 6 N. H. 247 (1833). Clorinda Doty owned a cow, two sheep, and a lamb. Her father, Daniel Doty, without any authority, sold and delivered them to G. & E. A. Webb, who turned them over to William Hawkins for safe-keeping. Clorinda Doty notified Hawkins that the animals were her property, and demanded them of him. Hawkins said that he had no doubt the animals were hers, but that she must go to the Webbs. She then sued Hawkins. *Held,* Hawkins was liable. The true owner having notified him of her claim, he was bound to restore the property to her, or to pay her its value.

(C) The bailor's obligations toward the bailee.

37. Except in the case of a gratuitous bailment, the principal duty owing by the bailor to the bailee is that of compensating him for his services. In most bailments the bailee performs some service for the bailor, the compensation for

which may have been fixed in the contract, or left unsettled with the understanding that it was to be a reasonable reward for the undertaking.

38. Where the bailee is entitled to remuneration, generally he has also the right to retain the bailor's property as security for the payment of his services in connection with it. This right is called a lien, and is implied by law in the case of most bailments where the bailee is to be compensated. Bailees' liens are of two kinds: (1) *particular liens,* which involve the right to retain the bailor's property on account of services rendered or money expended in connection with the bailment in question; (2) *general liens,* which involve the right to retain the bailor's property on account of a general balance due by the bailor. Unless otherwise agreed, a bailee's lien is usually only particular.

Owen *v.* Duhme, 3 Ohio Dec. 303 (1858). Owen bought a watch from Duhme, paying part of the purchase price and getting credit for the balance. Afterwards he left the watch to be repaired. When he called for it he was told he could not have it unless he should pay the rest of the purchase money. Owen sued for the return of the watch. *Held,* when Duhme received the watch back for repairs he was a bailee, and after being paid for the repairs he could not hold the watch as security for the payment of any other debt due by Owen. Therefore, Owen was entitled to his watch.

Firth *v.* Hamill, 167 Pa. 382 (1895). Firth & Foster Brothers had dyed clothes for Hamill for several years. On their bills, invoices, and other business stationery appeared this notice, "All goods received only upon condition that they are subject to a general lien, not only for the dyeing and finishing thereof, but also for the balance of any former amount due." Hamill disputed the right of Firth & Foster Brothers to hold certain goods for anything but the charges due on those same goods. *Held* that as Firth & Foster Brothers had a general lien, they could hold the goods for all sums due them. One who is not bound by law to receive bailments may stipulate the conditions on which he will take another's property, and Hamill had every reason to know that Firth & Foster Brothers received the goods subject to a general lien.

39. In order that a bailee may assert a lien against property, usually it must be in his exclusive possession. Possession is essential to the existence of a lien, and, therefore, if the bailee voluntarily parts with the possession, he loses his lien.

He may also waive his right to a lien and make himself liable as a wrongdoer by dealing with the goods as his own, or by a general refusal to deliver them up without stating that he retains the goods for the amount of the lien.

Hurley & Smith *v.* Epps, 69 Ga. 611 (1882). Hurley & Smith had a lien for some repair work on a buggy. They permitted the sheriff to seize the buggy on another person's judgment against the owner without notifying him of their claim. Later they sued to establish their lien. *Held*, by allowing the sheriff to take possession of the buggy without asserting their claim, they had lost their lien.

(D) The bailor's obligations toward third parties.

40. Ordinarily bailment contracts do not bring the bailor into legal relations with third parties. The bailor is not liable to third persons for injuries resulting from the bailee's negligent use of the property. For this reason in many cases it is more desirable for the owner of property to create a bailment rather than an agency relation.

Felton *v.* Deall, 22 Vt. 170 (1850). Deall hired her ferry-boat for a year to a man named Hobbie. By reason of Hobbie's negligent management of the boat Felton was injured. He sued Deall. *Held* that Deall was not responsible for the negligence of her bailee.

(E) Obligations of third parties toward the bailor.

41. The bailor does not lose his title to the property by transferring the possession to a bailee. Therefore, he may sue third parties for interfering with the bailee's possession or for any damage to the thing bailed. So also if a bailee, in violation of the terms of bailment, sells the property to a third person who purchases in good faith and in ignorance of the bailor's rights, usually the bailor is entitled to the property as against the third person and any one claiming under him.

Ingersoll *v.* Emmerson, 1 Ind. 76 (1848). Ingersoll owned the canal boat *Gideon*, which he lent to Gideon Halloway in order that Halloway might operate the boat on the Ohio Canal and apply the profits to the payment of a debt owing by Halloway to him. Halloway sold and delivered the boat to Emmerson. When Ingersoll learned of this, he sued Emmerson to recover the boat. *Held*, Ingersoll should get his boat, for Halloway was a bailee for a particular purpose, and could not, in disregard of that purpose, sell the property even to a purchaser in good faith without notice of Ingersoll's rights.

(F) Obligations of third parties toward the bailee.

42. The right of the bailor of personal property is that of ownership. The right of the bailee is that of possession. The bailee's right of possession entitles him to sue a third party who maliciously or negligently injures the property while in his charge. Thus he may sue if the property is lost or injured through the negligence of a common carrier or innkeeper, or if it is wrongfully appropriated by a third person. He may recover not only for the damage which he suffers by reason of being deprived of the full use of the article, but also for all injuries caused to the property. The amount recovered by him in excess of his own interest he should hand over to the bailor.

GILLETTE *v.* GOODSPEED, 69 Conn. 363 (1897). Gillette borrowed a horse and wagon with which he embarked on Goodspeed's ferry-boat. The horse and wagon were destroyed, and Gillette sued Goodspeed for their full value. Held, if Gillette could prove that Goodspeed was negligent he could recover the full value of the property. But he could keep only enough to repay the loss suffered by himself as bailee, and must account to the owner for the balance.

THE TRANSPORTATION OF PERSONAL PROPERTY

43. Our main topic under the head of the transportation of personal property will be the carriage of goods by a common carrier. Incidentally, the law relating to personal baggage of passengers on railroad trains will be discussed. There are many different methods by which a bailee may transport personal property from one place to another. If he is not a common carrier, his liability is to be determined according to the rules laid down in Arts. **29** to **41.** Most of the transportation business is, however, in the hands of common carriers, who are subject to greater liability than the ordinary bailee; hence the necessity of treating this topic separately.

(A) Who is a common carrier?

44. A common carrier is one who holds himself out as being ready to carry for hire the goods of all persons that may employ him. A private carrier is one who agrees in a special case to transport personal property. The distinction between

the two is that a common carrier of goods pursues the business of transportation as his calling or occupation, and undertakes to carry any person's goods within the limit of his facilities. On the other hand, a private carrier only undertakes the transportation of goods in special cases or for certain particular parties.

VARBLE *v.* BIGLEY, 77 Ky. 698 (1879). Varble, who was engaged in the towboat and jobbing business, sued to recover compensation for towing a coal boat. Bigley defended on the ground that, while in Varble's charge, the coal boat had sunk. The case hinged on the question whether or not Varble was a common carrier, it being agreed that if he was, he could not recover in view of the heavy liability laid on such carriers. *Held* that Varble was a private carrier and, therefore, was entitled to his compensation. Varble's business was such that the public could not reasonably suppose that he would tow for all who might offer. He did not operate on a definite route or between established terminals. Therefore, he could not be regarded as a common carrier.

BAKER *v.* MAHER, Howell N. P. (Mich.) 39 (1880). At a railroad station Baker intrusted her trunk to Maher, an expressman who habitually carried baggage to and from trains. Maher was to deliver the trunk at Baker's home, but on the way it was stolen. Baker sued him for the value of the trunk and its contents. *Held,* she could recover, for Maher was a common carrier and, therefore, liable in such cases.

45. Ordinarily, we think of railroad and express companies as the only common carriers. But the following have also in most cases been held to be common carriers: canal and pipe-line companies, proprietors of stage coaches and omnibuses, hackmen and cabdrivers, ferrymen, proprietors of steamships, schooners, barges, canal boats, and other vessels used for the transportation of goods for the public.

46. The United States Statute of June 29, 1906, regulates interstate transportation. It provides that the term "common carrier" as used in the act shall include sleeping car companies. But such companies are usually not common carriers as regards transportation exclusively within the limits of a state.

(B) Duty to receive and carry.

47. Under certain limitations a common carrier is obliged to receive and transport goods of whatever kinds he holds himself out as ready to carry, provided he has room for them.

If he professes to carry only merchandise, he cannot be compelled to carry live stock. If he limits his obligation to transportation between New York and Chicago, he cannot be forced to carry from New York to San Francisco. No common carrier is required to provide other means of transportation than it owns or uses or holds itself out to the public as owning or using. Thus, it would be unreasonable to expect a local express company, which delivers goods by wagon from one point to another in a city, to transport goods by railroad from one town to another.

48. In order to force an unwilling carrier to transport goods, the shipper must tender the transportation charges in advance. If the goods are dangerous, improperly packed, or otherwise unfit for shipping, the carrier may refuse to receive them. Neither, as a rule, is he obliged to accept goods when he has not sufficient facilities for handling them. But, by statute, in many jurisdictions, railroad companies must provide sufficient facilities to handle all the traffic reasonably to be anticipated. A common carrier must not unjustly discriminate between his customers. He should carry indifferently for all who offer, and, under like conditions, give all the same terms and equal facilities.

(C) Delivery to carrier.

1. What Amounts to Delivery?

49. The carrier's liability does not rise until the goods have been delivered to and accepted by him. The delivery must be made to the carrier or his authorized agent, and the goods must be in his exclusive custody and control. For example, in case a steerage passenger has possession and control of his trunk, the ship company would not be liable for a loss sustained by him through theft, to nearly the same extent as if the trunk were entirely in the company's charge.

50. If when the carrier has received the goods for the purpose of immediate transportation, he places them for his own convenience in storage, he is liable as a carrier. But if, after receiving the goods for transportation, he delays ship-

ment for the owner's convenience, his liability is only that of a warehouseman.

Pine Bluff Ry. Co. *v.* McKenzie, 75 Ark. 100 (1905). At McKenzie's request, and in accordance with its custom, the railway company left two cars on its side track, agreeing to haul them off next day if loaded. The same day the cars were loaded and closed, and notice to remove them was given to the conductor of a freight train. He promised to move them next day, but at three o'clock the next morning the cars and their contents were destroyed by fire. McKenzie sued the railway company for the value of his property which had been burned. *Held* that there had been a complete delivery of the freight contained in the cars to the railway company, which, therefore, was liable for the loss, even though no bill of lading had been executed.

2. Delivery to Connecting Carriers

51. A carrier is not required to accept goods for carriage beyond the terminus of his own line. On goods thus consigned, he may limit his liability to that of a forwarding agent in making delivery to the connecting carrier, ceasing to be responsible for the goods when such delivery is made. But the Act of Congress of June 29, 1906, forbids such limitation of liability in interstate shipments.

Illinois Central Railroad Co. *v.* Frankenburg, 54 Ill. 88 (1870). Frankenburg shipped goods over the Illinois Central Railroad Company from Bloomsburg, Illinois, to Columbus, Ohio, and paid freight to Pana. The Illinois Central delivered the goods to the Terre Haute & Alton Railroad Company at Pana. They were spoiled in transportation from Pana to Columbus, and Frankenburg sued the Illinois Central Railroad Company. The bill of lading limited the liability of that company to its own line. *Held,* if a common carrier accepts goods consigned to a point beyond its own line, generally it is responsible for their safe arrival at their destination. But by express contract it may limit its liability to the terminus of its own road, and Frankenburg could not recover from the Illinois Central. But see the Act of June 29, 1906, referred to above.

52. A carrier, by contract express or implied, may agree to carry to a point beyond the terminus of his own line. When he enters into an undertaking to carry the goods through to their final destination, all connecting lines of carriers are held to be his agents. He, therefore, becomes responsible to the shipper for loss or damage occurring on the connecting lines.

ELGIN, JOLIET & E. RY. CO. *v.* BATES MACHINE CO., 98 Ill. App. 311 (1901). The Bates Machine Company shipped a flywheel over the E. J. & E. line from Joliet, Illinois, to Louisville, Kentucky. At Dyer, Indiana, the E. J. & E. Railway Company delivered it to the Monon R. R. Company, by which company it was taken to its destination. While in the Monon Company's custody, the wheel was ruined, and the Bates Machine Company sued for its value. *Held* that the E. J. & E. Company was liable. The Bates Machine Company paid freight for transportation from the place of shipment to the final destination, and there was nothing in the bill of lading to limit the E. J. & E. Company's responsibility to injuries occurring on its own line. The acceptance by the E. J. & E. Company of the flywheel for transportation to a point beyond its own line showed a contract to carry and deliver the freight to the point of destination.

(D) Bills of lading.

53. A common carrier's liability is created in large measure by law, and does not arise entirely from contract. Once the goods have been delivered to and accepted by him, his liability for them attaches. No writing of any kind is required to make him liable as an insurer. However, usually a bill of lading or a shipping receipt is issued to the shipper. This bill of lading or shipping receipt is both a receipt and a contract. So far as it acknowledges the delivery and acceptance of the goods it is a receipt. So far as it provides for the terms and manner of shipment and the carrier's liability, it is a contract. As a receipt it is good, but not always conclusive, evidence that the carrier has received the articles mentioned in it. See Arts. **54-55,** and Part 3, Art. **82.**

(E) Duty to carry safely; discrimination.

54. Having received the goods, the carrier is liable for their safety. The general rule is that a common carrier is an insurer against loss or injury occurring in any way except through (1) the act of God, (2) the public enemy, (3) the shipper's fault, or (4) defects or qualities of the goods themselves. Of course, if the goods are seized by the public authorities, as, for example, animals infected with contagious diseases, the carrier is not liable as an insurer.

55. Except in a few states, common carriers, by contract with the shipper, may limit their liability to a certain extent.

Usually the terms of such contract are included in the bill of lading. See Art. **52.**

56. The law does not allow a carrier to free himself from the consequences of the fraud or felony of himself or his servants. Neither does it allow him, except in New York, to contract for exemption from any liability for loss due to his own or his servant's negligence. Save as above, however, he can exempt himself from any liability which may arise out of the risks incident to transportation.

Missouri Valley R. Co. *v.* Caldwell, 8 Kans. 244 (1871). Caldwell shipped a mirror over the Missouri Valley Railroad. The bill of lading provided that the mirror should be at Caldwell's risk as regarded breakage. While in the railroad company's charge it was placed on a levee, along with agricultural implements and other heavy freight, in a narrow passageway through which drays passed. Being thus exposed, it was struck, overturned, and broken. Caldwell sued for its value. *Held,* the bill of lading operated only to relieve the carrier from his liability as an insurer. But it left him liable for lack of ordinary care, the same as most bailees for hire. He clearly displayed a want of such care, and was bound to pay Caldwell for the mirror.

57. The carrier is allowed by contract with the shipper to put a maximum value on the goods beyond which the carrier shall not be held liable in case of loss. If the goods are worth more than the maximum value usually set, the shipper at the time of delivery must state what they are worth, and pay extra for having them transported proportionately to such increased valuation.

58. In the contract, the carrier may limit the period within which claim shall be made upon him by the owner of the goods in case of loss, provided the owner is given a reasonable time. The object of such stipulation is to enable the carrier to look into the matter while it is still fresh.

59. Common carriers are not allowed to discriminate between customers in the transportation of either freight or passengers. They must carry indifferently for all that offer. They cannot give preference to some, or make unequal charges, but must charge all equally for similar services, and carry for all persons who apply in the order of their application.

They are subject to an action for damages for a refusal to carry when they have facilities, or for discriminating in favor of some of their patrons to the detriment of others.

(F) Custody and control of the goods, and rights in them.

60. Common carriers are entitled to a reasonable compensation for their services. They cannot be compelled to carry gratuitously. Neither may they charge exorbitantly high rates for transportation. Usually the carrier's charges are fixed by contract. If there is no contract the carrier is entitled to the usual or customary charge. In the absence of a customary rate, the carrier may recover a reasonable compensation. The rate may be fixed by statute. A statute fixing a maximum rate which is unreasonably low amounts to a confiscation of the carrier's property without due process of law, and is, therefore, unconstitutional.

61. The carrier may demand his compensation in advance, and refuse to accept goods unless prepaid. If the goods are not prepaid he may claim his freight after he has carried them and is ready to deliver them. The shipper is originally liable to pay freight. But if the consignee accepts the goods, the law presumes that he owns them and makes him liable for the freight. The law gives the common carrier a lien for the whole amount of the freight upon every part of the goods. Therefore, if a part of a shipment has been delivered, the carrier may retain the balance until his entire freight has been paid.

62. Carriers by water generally contract for the payment by the consignee of a certain sum for each day the carrier is detained by reason of the consignee's failure to receive the goods. This charge is called demurrage. Railroad companies usually discharge their own cargoes and have warehouses in which to store them. If the consignee fails to receive the goods promptly, he is liable for warehouse charges. Where goods are delivered to the consignee in the carrier's railroad cars, the carrier may charge a reasonable compensation for

the use of his cars if the consignee keeps them longer than is proper.

63. In addition to his right to compensation, the carrier has certain other rights in respect of the goods. He may maintain an action against any one who seizes or damages the goods while they are in his possession. He has an insurable interest in them, and, therefore, may insure them to their full value. In certain emergencies, as where perishable fruit is about to spoil, the carrier may sell the goods.

(G) Termination of liability; delivery by carrier.

64. Generally, the requisites of a valid delivery by the carrier are three. It must be made (1) at a reasonable time, (2) at a proper place, and (3) in a proper manner. If the delivery does not contain these requisites, the carrier will not be relieved of his responsibility for the safety of the goods. Circumstances of time, place, and manner, as well as of the person to whom delivery is made, are of great importance in determining whether or not the carrier's delivery has relieved him of his extraordinary liability.

Singer *v.* Merchants Despatch Transportation Co., 191 Mass. 449 (1906). Louis Singer of Boston shipped goods to himself at Springfield, Illinois, naming the consignee, "L. Singer." The transportation company's contract did not require the production of a shipping receipt or a bill of lading upon delivery of the goods to the consignee. Lena Singer of Springfield, who did business as L. Singer and who was known to the carrier, demanded the goods. They were delivered to her, though she did not present either a bill of lading or a shipping receipt. Louis Singer sued for the value of the goods. *Held,* the carrier performed his contract by delivering the goods to L. Singer, and was not liable. Louis Singer had failed to tell the carrier that he meant the goods for L. Singer of Boston and not L. Singer of Springfield.

1. Delivery by Carriers by Water

65. Ordinarily carriers by water are not obliged to deliver goods personally to the consignee. All that is required of them is that they shall land the goods upon the wharf or other proper place, and notify the consignee. It is then the consignee's duty to take them away, and if he does not do so in a reasonable time, the carrier may put them in storage for the consignee, and at the consignee's risk and expense.

2. Delivery by Railroad Companies

66. There is no uniform rule regarding the delivery required of railroad companies in order to change their liability from that of insurers to that of ordinary bailees for hire. Railroad companies are nowhere required to deliver freight to a consignee's place of business not connected with their tracks, but the states differ as to what circumstances constitute performance of a carrier's contract to deliver freight at the point of destination.

67. In Georgia, Illinois, Indiana, Iowa, Massachusetts, Missouri, North Carolina, Pennsylvania, and South Carolina the rule is that a railroad company is required only to deposit the goods in safety upon its station platform, or in its warehouse, to await delivery to the consignee when he shall call for them. The carrier is under no duty to notify the consignee of the arrival of the goods. From the time of their deposit at the point of destination the carrier's liability is changed from that of an insurer to that of a warehouseman, and he is liable only for the degree of care required in the case of ordinary bailments for mutual benefit. This rule is based on the assumption that the consignee has been notified by the shipper or in some other way that the goods are in transit, and that he can calculate approximately the time of their arrival, whereupon it is his duty to call for them.

Norway Plains Co. v. Boston & Maine Railroad Co., 1 Gray (Mass.) 263 (1854). The Norway Plains Company delivered to the railroad company at Rochester, N. H., certain goods to be shipped to Boston. They arrived in Boston on time and were taken from the cars and placed in the company's warehouse. No notice of the arrival of the goods was given to the Norway Plains Company or to its agent. During the night the warehouse burned down and the goods were destroyed. The fire was not due to any negligence on the part of the railroad company. The Norway Plains Company then sued for the value of the goods. *Held* that the railroad company was not liable as a common carrier. Its contract was only to carry the goods safely to the place of destination and there to put them on the platform, and to deliver them to the consignee if he was there to receive them; or if the consignee was not there, to place them securely and keep them a reasonable time to be delivered when called for. It had fulfilled its contract by storing

the goods in its warehouse, and could not be held liable as a common carrier for their destruction by fire.

68. In Arkansas, Kansas, Kentucky, Louisiana, New Hampshire, Vermont, West Virginia, and Wisconsin the railroad company is not obliged to notify the consignee of the arrival of the goods. But when the railroad company has put the goods on its station platform or stored them safely in a suitable warehouse, it remains liable as an insurer until the consignee has had a reasonable opportunity to remove the goods.

Moses *v.* Boston & Maine R. R. Co., *32* N. H. 523 (1856). Moses delivered ten bags of wool to the railroad company at Exeter, N. H., to be transported to Boston. The train on which the wool was loaded arrived in Boston and the wool was transferred to the railroad company's warehouse at about three o'clock in the afternoon. Generally, two or three hours were required to unload the freight from the cars into the warehouse, and the gates of the yard were closed at five o'clock, so that no goods could be removed from the warehouse after that hour until the next morning. During the night the warehouse and its contents, including the wool, were destroyed by fire. Moses sued the railroad company for the value of the wool. *Held* that the railroad company was still liable as a common carrier, and hence must pay Moses the value of the wool. The liability of railroad companies as common carriers continues until the goods are delivered at the point of destination and the consignee has had a reasonable opportunity to remove them.

69. In Alabama, California, Michigan, Minnesota, Mississippi, New York, Ohio, Tennessee, and Texas it is held that if the consignee is not actually present at the point of destination the carrier, in order to terminate his liability as insurer, must give the consignee notice of the arrival of the goods, and allow him a reasonable time in which to remove them.

Sprague *v.* New York Central R. R. Co., 52 N. Y. 637 (1873). Sprague delivered to the railroad company at Fonda, N. Y., goods consigned to the American Express Company at Albany, N. Y. No notice of their arrival at Albany was given to the express company. Sprague sued for injuries to the goods caused three days after their arrival by a heavy freshet which overflowed the freight house where they had been stored. *Held,* it was the railroad company's duty to give notice of the arrival of the goods. As it had failed to do so, its liability as a common carrier continued, and it was bound to make good Sprague's loss.

3. Delivery by Express Companies

70. Express companies do a different business from that of railroad companies. For the most part they carry small and valuable packages. They undertake to make delivery to the consignee personally, and the law holds them to this undertaking with great strictness. However, at unimportant way stations, where they have no facilities for local delivery, they need only notify the consignee of the arrival of the goods and give him a reasonable length of time to call for them.

(H) Baggage.

71. Carriers of passengers are obliged to receive the baggage of their passengers. Their liability with respect to it is that of insurers. The passenger is entitled to have a reasonable amount of baggage carried as incidental to the contract to carry him. The price paid for his ticket is the consideration for the transportation of both, provided the passenger has his baggage ready for shipment in time to go in the same train that he himself takes.

72. There is no hard and fast rule as to what may be considered "baggage." In general terms, "baggage" signifies those articles of convenience or necessity which are ordinarily carried by a passenger for his personal use during the journey or on arriving at his place of destination, and such as individuals in a similar station of life would commonly have. This would include not only articles of apparel, but also in proper cases guns for sporting purposes, the tools of a mechanic, the easel of an artist on a sketching tour, the books of a student, a watch and a reasonable supply of jewelry intended to be worn by the traveler on his journey, as well as other articles of an analogous character. What is carried for purposes of business, such as merchandise, or for household use, such as furniture, is not ordinarily regarded as baggage unless accepted as such by the carrier.

Railroad Co. *v.* Baldwin, 113 Tenn. 205 (1904). Baldwin, a livery stable keeper, bought a ticket for his wife to Helena, Ark., from Jonestown, Miss. He and his wife were journeying to Helena for the purpose of making it their home. One of the wife's trunks contained

a small quantity of her husband's clothing. The trunk and its contents were lost, and suit was brought against the railroad company. *Held* that it was liable for the trunk and its contents including the husband's clothing. It is customary for a wife of the station and condition in life of Mrs. Baldwin to pack in her trunks a few articles of her husband's clothing when they are traveling together.

Nevins *v.* The Bay State Steamboat Co., 4 Bosw. (N. Y.) 225 (1859). Nevins was a passenger on the defendant's steamboat *Metropolis*. His trunk contained certain jewelry, Masonic regalia, and engravings. During the trip the trunk was lost, and Nevins sued the steamboat company for the value of these articles. *Held* that the carrier was not liable. The contents of the trunk were not intended for the personal convenience of the traveler on the journey, and were not properly baggage.

AMERICAN BUSINESS LAW

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SALES AND MORTGAGES OF PERSONAL PROPERTY

THE DEFINITION OF A SALE, AND THE DISTINCTION BETWEEN SALES AND BAILMENTS

1. When a sale takes place, the title to property passes from one person, called the seller, to another, called the buyer or purchaser. By the passage of title, the buyer becomes the owner of the property sold. Sometimes the seller is called the "vendor," and the buyer is called the "vendee." A sale is defined in Art. **4.**

2. The rules to be discussed apply not only to sales of tangible articles of personal property, such as books or automobiles, but to sales of intangible personal property as well. Intangible personal property includes such rights as patents, copyrights, trade-marks, trade-names, and other forms of advertisement.

3. In purchasing certain kinds of property care should be taken to observe the various statutory provisions with regard to recording. For example, unless an assignment, grant, or conveyance of a patent is recorded in the United States Patent Office within three months, it will not be good as against a subsequent purchaser without notice thereof. Recording is not necessary to pass title as between the parties, so that an unrecorded assignment is good as against every one but a sub-

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sequent purchaser without notice. But suppose that A assigns a patent to B, who fails to record the assignment within three months. If after that period A assigns to C, who promptly records his assignment, having no notice of the prior one, C's title will be good as against B. See Art. **72.**

(A) The formation of a contract of sale.

4. A sale is a transfer by which one party passes the ownership of property to another in return for money, or a promise to pay money. A sale differs from a barter, since in the former the consideration is money, while in the latter it is some other kind of property.

5. Sales, being based on contract, are subject to the rules of contract law. When the buyer acquires the right of property immediately upon making the contract, it is called an *executed* contract of sale. When he is to acquire the right of property at some time in the future or upon the performance of a condition, the contract is said to be *executory*. The fact that the buyer has acquired the right of property is generally shown by a delivery of the thing sold. But the parties may agree that while the buyer is to acquire the right of property, the seller is to retain possession until all or part of the purchase price has been paid.

MIDDLETON *v.* BALLINGALL, 1 Cal. 446 (1851). Ballingall agreed to sell Middleton certain goods then being forwarded from Java to San Francisco. It was stipulated that the contract should not be considered binding until the ship's arrival. The ship never arrived, and Middleton sued Ballingall to recover damages for the non-delivery of the goods. *Held* that Middleton could not recover. The contract was executory, and the fulfilment of it depended on the contingency of the ship's arrival.

6. A valid contract of sale must, of course, contain the five elements necessary to every contract. The following requisites must also be present in the agreement: *first*, the subject-matter of the agreement which is owned in most cases by the seller; *second*, an agreement by the parties that the property in the thing is transferred or is to be transferred from the seller to the buyer; *third*, payment or an agreement for payment of a price in money by the buyer to the seller. The con-

tract need not be in writing, but may be made verbally or implied from the conduct of the parties, except as noted in Part 2, Arts. **76** and **77.**

A form of bill of sale in general use is shown in Fig. 1.

KNOW ALL MEN BY THESE PRESENTS that I, Roger Thorn, of the city of Buffalo, Erie County, State of New York, of the first part, for and in consideration of the sum of Five Hundred Dollars ($500), lawful money of the United States of America, to me paid at or before the sealing and delivery of these presents, by Levi Webb, of the same city, of the second part, the receipt whereof is hereby acknowledged, have bargained and sold and by these presents do grant and convey unto the said party of the second part, his executors, administrators, and assigns, my iron gray horse known as Random.

TO HAVE AND TO HOLD the same unto the said party of the second part, his executors, administrators, and assigns forever. Furthermore, I covenant with the said party of the second part that I own and have the right to sell and transfer the said property, and that I will defend the same against any person or persons whomsoever claiming the same.

IN WITNESS WHEREOF I have hereunto set my hand and seal the sixteenth day of June in the year one thousand nine hundred and twenty-one.

[*Signed*] ROGER THORN (SEAL)

In the presence of
[*Signed*] JAMES MACDONALD

STATE OF NEW YORK,
COUNTY OF ERIE } *ss.:*
CITY OF BUFFALO.

On this sixteenth day of June in the year one thousand nine hundred and twenty-one before me, the subscriber, personally appeared Roger Thorn, to me personally known to be the same person described in and who executed the foregoing instrument, and he acknowledged to me that he executed the same.

[*Signed*] TERESA MANGANO,
Notary Public for Erie County, New York.

(NOTARIAL SEAL)

FIG. 1

(B) Sales and bailments distinguished.

7. A bailment of property should be carefully distinguished from a sale. In a bailment, the bailee gets possession of the thing, but he does not get the right of property or title to the thing, which remains in the bailor. In a sale the transfer is of the property itself; the ownership is passed from seller to buyer, and the possession may or may not be transferred.

THE TRANSFER OF TITLE FROM SELLER TO BUYER

8. In this chapter we shall consider, *first,* when the title passes by virtue of a contract of sale, and, *second,* what title is acquired by the purchaser.

(A) When the title passes to the buyer.

9. It is often important to decide the exact moment when the contract of sale passes the rights of property from seller to buyer. As a rule, the passage of title determines who shall bear the risk of loss by fire or other causes incident to the ownership of goods. Generally the right of property passes at the time when the parties intend that it shall pass. The contract of sale may definitely express the intention of the parties as to the passage of title. If it does not do so, what the parties probably had in mind is to be ascertained from a consideration of the particular circumstances of each case.

Morgan *v.* King, 28 W. Va. 1 (1886). King sold Morgan all of King's merchantable timber at certain places. Nothing was said about examining and measuring it, but Morgan spent a short time in sawing part of the timber into logs. Then he became sick, and during his sickness the timber was swept away by a flood. King sued Morgan for the price of the timber. *Held* that King was entitled to recover. The circumstances made it clear that the parties intended title to pass at once to Morgan. Therefore, the loss was Morgan's and not King's.

10. Usually title is held to pass at the moment when the seller delivers the goods to the buyer. If the seller delivers the goods to a common carrier for transportation, the carrier is generally regarded as acting for the buyer, and title passes to the buyer when the goods are delivered to the carrier. The buyer ordinarily pays the freight. The carrier is thus his bailee, and the contract is performed when the seller delivers the goods to the buyer's bailee. But if the seller agrees that he will deliver the goods at a certain place, the carrier who takes them there is his bailee, and the buyer does not become the owner until the goods are delivered at the place agreed upon.

GATES *v.* CARQUINEZ PACKING CO., 78 Cal. 439 (1889). Under a contract for the sale of fruit, the packing company was to deliver it on cars consigned to Gates, and to send daily statements of weights. The fruit was to be reweighed on arrival at the cannery, and, in case of difference, the weight was to be adjusted. In a suit for the price of a shipment, the question arose as to who must suffer the loss caused by shrinkage in transit. *Held* that title passed on delivery to the carrier, and loss from shrinkage during transit must be borne by the buyer.

11. Where there is merely a contract to purchase at a future time, the buyer does not acquire title when the contract is made. While anything remains to be done by a seller, usually title will not pass, as where the seller is required to ascertain the identity, quantity, or quality of the article sold, or to put it in the condition called for by the contract.

12. Where the goods bought are a certain quantity from a larger bulk of uniform kind and quality, the property may pass even though there is no designation of the particular parts to be sold or any separation of them from the bulk, if such is the intention of the parties. But this rule applies only where the larger quantity is composed of uniform parcels, and not where the parcels differ in quality or possess a distinct individuality. For example, 1,000 bushels of wheat may be sold out of a mass of 8,000 bushels stored in a grain elevator without designating the particular 1,000 bushels which the buyer acquires by the contract.

(B) What title passes to the buyer.

13. As a general rule, the seller of personal property can give no better title than he himself has. Therefore, if you buy goods from a thief or a mere bailee, you cannot usually acquire a greater interest therein than the seller had. Certain exceptions to this rule will be treated under the following subdivisions. See also Art. **19.**

1. NEGOTIABLE INSTRUMENTS

14. When a negotiable instrument is transferred in due course to a holder in good faith and for value, he usually acquires a clear title thereto, although the seller's title may have been defective. See Part 3, Art. **18.**

2. Where the Owner Deceives Third Persons as to the Title

15. An owner of property may be estopped by words or conduct from attacking the buyer's title if he has wilfully caused the buyer to believe that the goods belong to a third person whom the buyer pays for the goods in reliance on such belief. This is on the principle that where one of two innocent persons must suffer by reason of a third person's fraud, the loss should fall on him who enabled the wrongdoer to perpetrate the fraud.

3. Two Purchasers of the Same Goods

16. Suppose that after a man bought certain goods he allowed them to remain in the possession of the seller, who thereupon sold and delivered them to a second purchaser. Suppose the latter paid for the goods in ignorance of the prior sale. Since the first purchaser's conduct in leaving the goods with the seller has enabled the latter to mislead the second purchaser by his statement that he still owned them, the second purchaser gets a good title. If the second purchaser also allows the goods to remain with the dishonest seller, who afterwards delivers them to the first purchaser, the latter may hold them as against the second purchaser. Where both parties are equally negligent, the one who has possession may keep it.

Hight *v.* Harris, 56 Ark. 98 (1892). Hight bought a mule from Largent, to whom he paid the price. The mule was to be delivered afterwards. Later the same day Largent sold the animal to Harris, who paid for it and took immediate possession in ignorance of the prior sale to Hight. Hight sued to get the mule. *Held* that the retention of possession by the seller of personal property after the sale raises a presumption of fraud, as against one who afterwards buys the property in good faith. Therefore, Hight lost his case.

THE RIGHTS OF THE SELLER OF PERSONAL PROPERTY

17. The seller's rights depend largely upon the terms of the agreement he has made with the buyer. Certain phases of contract law which particularly concern sales of personal property will be treated in this chapter. We shall consider, *first,* the seller's right to set aside the contract if the buyer has committed fraud; *second,* the seller's lien for the purchase money, or right to refuse delivery until the purchase money has been paid; *third,* the seller's right of stoppage in transit.

(A) The seller's right to set the contract aside if the buyer has committed fraud.

18. When one party has been induced to enter into a contract by the other party's fraud, the contract is voidable at the option of the party defrauded. Fraud is a false representation of fact made with knowledge that it is false, or in reckless disregard as to whether it is true or false, with the intention that it shall be acted upon by the complaining party, and actually inducing him to act. See Part 2, Art. **38.**

19. Let us imagine that the owner of goods is defrauded into agreeing to sell them by the purchaser's false representations. If the seller learns of the fraud before he has delivered the goods to the buyer he may refuse to go ahead with the transaction. But suppose that, after the goods have been delivered to the purchaser on credit, the seller learns that the former's statements as to his financial condition were untrue. If, in the meantime, the defrauding buyer has sold the goods to an innocent third party, the latter gets a good title and the original seller cannot reclaim the goods from him.

Kern & Loeb *v.* Thurber & Co., 57 Ga. 172 (1875). Kern & Loeb sold eleven barrels of sugar in New York to Barnard & Co., of Columbus, Georgia, who fraudulently induced Kern & Loeb to sell them on credit. Before the goods arrived in Columbus, Kern & Loeb learned that Barnard & Co. were insolvent. They failed in an attempt to stop the goods in transit. When the sugar reached Columbus it was sold and delivered by Barnard & Co. to Thurber & Co. Kern & Loeb sued Thurber & Co. to recover the sugar. *Held* that Thurber & Co.

had a good title. Though the title of Barnard & Co., having been obtained by fraud, was voidable, Thurber & Co. were innocent purchasers without knowledge of this fraud.

20. If, however, when the seller learns of the buyer's fraud, the goods are still in the latter's possession, the seller has two courses of action open to him. He may enforce the contract, or he may rescind it. Generally the latter procedure is adopted. The seller should be careful lest he waive his right to set the contract aside on the ground of fraud. If, after discovering the fraud, he sues for the purchase price, or takes a note for it, or proves his claim for the price in insolvency proceedings, he loses his right to rescind the contract. Ordinarily the seller should disaffirm the agreement of sale, alleging that it was not a genuine contract, because it lacked reality of consent, the fourth element necessary to every contract. He should bring an action to recover the goods on the ground that he has a right to have the sale annulled, and the goods restored to him.

Levi *v.* Kraminer, 2 Ind. App. 594 (1891). Levi falsely represented to Kraminer that he was solvent and doing a prosperous business. Kraminer, relying on this representation, sold him goods on four months' credit. When Kraminer learned that Levi's statements were false, he sued him to recover the property. *Held* that if one, knowing himself to be insolvent, obtains goods on credit by falsely representing his financial condition, the seller may set aside the sale and recover the property. Therefore, Kraminer was entitled to the goods, although the four months had not elapsed when he brought suit against Levi.

21. Ordinarily where one person falsely passes himself off for another, or falsely represents himself to a seller as the agent of another individual, and the seller, misled thereby, sells and delivers goods to him, the imposter does not acquire title by the trick.

Rodliff *v.* Dallinger, 141 Mass. 1 (1886). Rodliff, on the representation of Henry Clementson that he was acting for a manufacturer who was in good credit with Rodliff, agreed to sell him a quantity of wool and took Clementson's note in payment. Clementson pledged the wool with Dallinger to secure a loan. Before Clementson's note fell due Rodliff discovered that Clementson had not been acting as an agent but on his own account. Thereupon Rodliff sued Dallinger to recover the wool. *Held,* since Clementson was not acting for the manu-

facturer, but for himself, there was no sale. Clementson, not having any title, could convey none even to an innocent purchaser or pledgee, and Rodliff was entitled to the wool as against Dallinger.

22. All the states have laws which help keep merchants from suddenly disposing of their goods in bulk and eluding their creditors. These laws, which are known as Bulk Sales Acts, vary in some particulars. Many of the Bulk Sales Acts provide that a sale by a merchant of his whole stock, or a large part of it, in a single transaction and out of the ordinary course of trade, shall be deemed fraudulent unless his creditors are notified of his intention to make such sale, a certain length of time before the sale is consummated.

(B) The seller's lien to secure payment of the purchase money.

23. In a cash sale, after the title to the goods has passed to the buyer, the seller, if he still retains possession of them, may refuse delivery until paid the purchase price. Suppose, for instance, that title has passed to the buyer, but that the seller is to hold the goods until the buyer needs them. If the sale is not on credit, the seller has a lien on the goods to secure payment. Suppose that the sale is on thirty days' credit, and at the expiration of that time the goods are still in the seller's hands and his bill has not been paid. In that case his lien would then revive. Or, if during the period of credit the buyer became insolvent, the seller's lien would revive, if he still had the goods.

Arnold *v.* Delano, 4 Cush. (Mass.) 33 (1849). Delano sold lumber to Arthur Sowerby, agreeing that Sowerby might remove it at any time within a year. He gave Sowerby a bill of sale and received Sowerby's promissory note for the price payable in six months. Before six months passed Sowerby became insolvent. His assignee, Arnold, sued Delano to recover the lumber. *Held,* Delano could retain the lumber until paid the price. There was a complete sale, but Delano had a lien for the price. By giving credit, he waived his lien, but only on the implied condition that Sowerby should keep his credit good. When Sowerby became insolvent, Delano's lien revived.

24. Unconditional delivery of the goods to the buyer or his agent terminates the seller's lien. But if a quantity of

goods is sold under a single contract, and the seller delivers some of them without being paid anything, his lien for the entire price remains on the goods still in his possession. In the case of a delivery to a common carrier the question whether or not the seller has waived his lien hinges on the point whether the common carrier is bailee for the seller or the buyer. Usually, the common carrier is regarded as the buyer's bailee, and hence, as a general rule, on delivery to the carrier the seller loses his lien. But if the seller has agreed to deliver the goods at the buyer's place of business or has reserved the right of disposal, the carrier is looked upon as the seller's bailee, and the seller does not lose his lien by delivery to the carrier. See Art. **10.**

25. Where the buyer fails to pay on time, and the seller still has the goods, he may not only refuse to deliver them unless paid, but may also, as a rule, drop the contract and sell his goods to another party. See Part 4, Art. **22.**

(C) The seller's right of stoppage in transit.

26. We have seen that where the seller delivers goods to the carrier as the buyer's bailee, he thereby loses his lien for the purchase money. But even though title has passed to the buyer, if he becomes insolvent before the goods are delivered to him by the carrier, the seller has the right of stoppage in transit. This enables him to resume possession of the goods if they are still in transit, and to keep them as security for payment of the purchase price. He should notify the carrier to hold the goods in time to prevent delivery to the buyer.

27. The right of stoppage in transit may be exercised only in case of the buyer's insolvency. The fact that the buyer has ceased to pay his bills in the usual course of business, or any other fact showing that he cannot meet his obligations, would justify the seller in directing the carrier not to deliver the goods to the buyer.

28. The seller may waive the right of stoppage in transit either expressly or impliedly. Again, the seller's right may be lost if the buyer has transferred a negotiable bill of lading to

a purchaser for value, who has taken it in good faith and without notice of the buyer's insolvency. See Part 3, Art. **82.**

29. The right of stoppage in transit relates only to the particular goods which are being transported. The seller may not stop in transit goods which have been paid for, in order to secure payment of what the purchaser owes him on other accounts.

THE RIGHTS OF THE BUYER OF PERSONAL PROPERTY

30. We may consider the purchaser's rights under two heads: *first,* his right to make the seller deliver goods of a certain kind and quality; *second,* his right to insist that a clear title to the property purchased must be transferred to him. There are numerous other rights which a purchaser may obtain under a contract of sale, but they do not require special treatment here. For instance, it is stated in Part 4, Art. **22,** that a provision in mercantile contracts as to the time of performance is usually an essential feature thereof. Hence, if the seller of goods in such a transaction fails to deliver them on time, usually the purchaser may refuse to go ahead.

(A) The buyer's right to get goods of a certain kind and quality.

31. The purchaser's rights for the most part group themselves around the idea that he should get what the seller agreed to give, in order that the contract may be properly performed. While this is true, it must not be inferred that the purchaser has a right to set aside the contract if the goods turn out to be less valuable than he expected. If he sees what he buys, usually he cannot return it merely because he learns later that it is of inferior quality. He has got what he bargained for, and the fact that he thought he was getting something very much better does not enter into the contract. The buyer should remember that in the ordinary sale transaction the maxim of the law is *caveat emptor,* which means, "let the buyer beware."

Therefore, he should judge for himself as to the value of the goods which are offered for sale and not be misled by anything the dealer may say in praising his wares.

1. Where the Seller Acts Fraudulently

32. It does not follow from this that the seller may make any statement he pleases about his goods. The law sets certain well-defined limits to the right of the seller to praise his wares. If, for example, he defrauds the buyer, the latter has a right to set the sale aside. The seller may freely express his opinion as to the qualities or characteristics of the article which he offers for sale, but if he misrepresents facts with the intention of deceiving the purchaser, the contract is voidable at the latter's option. See Part 2, Art. **38.**

Hicks *v.* Stevens, 121 Ill. 186 (1887). Hicks was the inventor of the "Hicks Tube Closer," which he represented to Stevens as a valuable invention. He assured Stevens that it would save 15 per cent. more steam than any other apparatus of its kind. Stevens, relying on Hicks's representations, bought the patent right. Later he discovered that Hicks's statements were false, and he sued to have the sale rescinded. *Held,* Hicks's representations related to matters of fact peculiarly within his own knowledge, and Stevens had a right to rely on them. As they were untrue the agreement was set aside.

Boles *v.* Merrill, 173 Mass. 491 (1899). Merrill sold Boles certain horses and wagons and the good-will of an express business. He represented to Boles that there were ten regular customers who each paid $10 a month, that another customer named Marble paid $60 a month, and that the business was earning $2,500 net yearly. When Boles discovered that these representations were false, he sued to have the sale rescinded. *Held,* the representations were not mere dealer's talk. They related to very material matters of fact, and Boles had a right to rely on them. Therefore, the agreement was set aside.

33. As a rule, it may be said that the seller's silence about the defects of his goods, or even his general assurance that the goods are all right, will not amount to fraud. Sometimes, however, the circumstances may be such that the purchaser is entitled to the benefit of whatever information the seller may have. See Art **37.** Where, for example, one employs an agent to purchase land of a certain character, and the agent offers to his employer land of his own, stating that it will

meet his employer's wants, the fiduciary relationship in which the seller stands to the purchaser binds him to tell all he knows against the suitability of the land for his employer's requirements. See Part 2, Arts. **36** and **37.**

2. Where the Seller Warrants His Goods

34. If a buyer intends to rely on the seller's representations as to the quality of the goods, he should be careful to make the seller warrant the truth of these representations. While the warranty need not be in writing, it is better to have it written if possible. The fact that the seller's statements have been put in writing may help to convince the court that the parties really considered them as warranties. If the same words were used verbally, the court might treat them as mere dealer's talk, not meant to be binding.

Worth *v.* McConnell, 42 Mich. 473 (1880). McConnell sued Worth for the price of a threshing machine. Worth defended on the ground that McConnell had told him the machine was "a very good machine and would do very nice work"; and that this constituted a warranty, which had been broken. *Held* that this statement was mere dealer's talk in praise of his wares, and McConnell, therefore, was entitled to recover, although really the machine was not very good, and did not do excellent work.

35. If the seller makes a definite assertion concerning his goods which is intended as a statement of fact, and which is so understood by the purchaser, who makes his acceptance of the goods depend upon the truth of the seller's statement, it will be held that the seller has warranted his goods. For example, a statement that tobacco was "sound, redried, and would certainly keep," has been held to be a warranty.

Stevens *v.* Bradley, 89 Ia. 174 (1893). At a public sale of hogs Bradley declared to the bidders that the hogs "were as thrifty and healthy a lot of hogs as the owner has ever owned in his life, and he has been in the business a good many years." Stevens bought twenty-seven of the hogs which he discovered later to be diseased. He then sued Bradley for breach of the warranty that the hogs were sound and healthy. *Held* that Stevens could recover. Bradley's statement was a material representation of fact. It was a distinct affirmation of health and soundness, and constituted an express warranty that the hogs were free from disease.

36. The article sold must be of the same kind as that contracted for. If the seller tries to substitute an article of an entirely different species from that called for by the terms of sale, he has failed to fulfil his contract, and the buyer may return the article. Where the bill of sale called for indigo and the article delivered was not indigo, but a different substance prepared so as to deceive even skilful dealers, it was held that there was a breach of the warranty that the article should be of the same kind as that contracted for, and that the buyer could return the goods.

37. There is a marked tendency to increase the seller's liability on implied warranties of quality. This is shown by the Uniform Sales Act, which has been adopted already by the following states: Arizona, Connecticut, Illinois, Maryland, Massachusetts, Michigan, Minnesota, Nevada, New Jersey, New York, North Dakota, Ohio, Pennsylvania, Rhode Island, Utah, Wisconsin, Wyoming, and Tennessee; also Alaska. Doubtless other states will adopt the Uniform Sales Act in the near future. The following three sections contain quotations from that act:

IMPLIED WARRANTY IN SALE BY DESCRIPTION

SECTION 14.—Where there is a contract to sell or a sale of goods by description, there is an implied warranty that the goods shall correspond with the description and if the contract or sale be by sample, as well as by description, it is not sufficient that the bulk of the goods corresponds with the sample if the goods do not also correspond with the description.

IMPLIED WARRANTIES OF QUALITY

SECTION 15.—Subject to the provisions of this act and of any statute in that behalf, there is no implied warranty or condition as to the quality or fitness for any particular purpose of goods supplied under a contract to sell or a sale, except as follows:

1. Where the buyer, expressly or by implication, makes known to the seller the particular purpose for which the goods are required, and it appears that the buyer relies on the seller's skill or judgment (whether he be the grower or manufacturer or not), there is an implied warranty that the goods shall be reasonably fit for such purpose.

2. Where the goods are bought by description from a seller who deals in goods of that description (whether he be the grower or manufacturer or not), there is an implied warranty that the goods shall be of merchantable quality.

3. If the buyer has examined the goods, there is no implied warranty as regards defects which such examination ought to have revealed.

4. In the case of a contract to sell or a sale of a specified article under its patent or other trade name, there is no implied warranty as to its fitness for any particular purpose.

5. An implied warranty or condition as to quality or fitness for a particular purpose may be annexed by the usage of trade.

6. An express warranty or condition does not negative a warranty or condition implied under this act unless inconsistent therewith.

IMPLIED WARRANTIES IN SALE BY SAMPLE

SECTION 16.—In the case of a contract to sell or a sale by sample:

(*a*) There is an implied warranty that the bulk shall correspond with the sample in quality.

(*b*) There is an implied warranty that the buyer shall have a reasonable opportunity of comparing the bulk with the sample, except so far as otherwise provided in Section 47, subsection 3.

[Section 47, subsection 3, reads as follows: Where goods are delivered to the carrier by the seller, in accordance with an order from or agreement with the buyer, upon the terms that the goods shall not be delivered by the carrier to the buyer until he has paid the price, whether such terms are indicated by marking the goods with the words "Collect on delivery," or otherwise, the buyer is not entitled to examine the goods before payment of the price, in the absence of agreement and proper written authority to the carrier permitting such examination.]

(*c*) If the seller is a dealer in goods of that kind, there is an implied warranty that the goods shall be free from any defect rendering them unmerchantable which would not be apparent on reasonable examination of the sample.

(B) Warranty of the seller's title.

38. Where a party who is in possession of goods sells them in his own right as absolute owner, the law generally implies a warranty on his part that he is the owner thereof and that he has a good title to the goods, even though he is silent on the question of his ownership, and whether or not he knew of any defect in his title. The sale is in itself an assertion of ownership. If the seller had no right to the property, the disappointed purchaser may recover the money which he has paid.

EXCEPTION.—Where the seller acts in an official capacity as sheriff, administrator, executor, guardian, or trustee in bankruptcy, he does not as a rule impliedly warrant the title to be in the party whom he represents.

CHATTEL MORTGAGES

39. A chattel mortgage is a conditional conveyance of personal property to secure the payment of a debt or the performance of some other obligation. The essential feature of a chattel mortgage is that upon performance of the conditions, the instrument becomes void. If the debt is not paid, or if any other obligation resting on the mortgagor is not performed, usually the mortgagee gets an absolute title to the thing mortgaged. If the condition is performed, the mortgage becomes void, and the mortgagee has no title. See Part 4, Art. **13.**

40. The subject of chattel mortgages is almost wholly regulated by the statutes of the various states, which differ widely from one another. Some states permit almost every kind of tangible personal property to be mortgaged, while others refuse to recognize such mortgages except in the case of a few specified articles.

41. Most states require that a chattel mortgage shall be in writing and signed by the mortgagor, the owner of the chattels. Moreover, it is usually necessary that a chattel mortgage be acknowledged by the mortgagor before a notary public or other similar official, and recorded in the county where the chattels are located. The requirement as to recording is made for the benefit of third persons, who are thus enabled to learn the nature and the extent of the mortgagee's rights. But an unrecorded chattel mortgage is ordinarily valid as against the mortgagor and as against third persons who have actually learned that the mortgage has been made. In drawing up a chattel mortgage, care should be taken to follow the form recognized in the state where the chattels are. In general, it may be said that the mortgage should carefully specify: (1) the name of the mortgagor; (2) the name of the mortgagee; (3) the exact nature, number, and location of the chattels; (4) the precise condition upon the fulfilment of which by the mortgagor the mortgage shall become void and the mortgagee's rights thereunder cease.

To all to Whom these Presents Shall Come, Greeting: Know ye that I, *Davis Coleman,* of *the City of Pittsburgh, County of Allegheny and State of Pennsylvania,* party of the first part, am indebted unto *Stephen Donovan,* party of the second part, in the amount of *Three Hundred Dollars, being for money loaned.*

Now for securing the payment of the said debt and the interest from the date hereof to the said party of the second part, the party of the first part does hereby sell, assign, and transfer to the party of the second part, the *500 barrels of Portland cement* contained in the property at *No. 78 Conestoga Street, Pittsburgh, Pa.,* the said cement now being and remaining in the possession of the party of the first part:

Provided Always, and this mortgage is on the express condition, that if the party of the first part shall pay to the party of the second part the sum of *Three Hundred Dollars* with interest at *six* per cent. within *one year* from the date hereof, which said sum and interest the party of the first part hereby covenants to pay, then this transfer to be void and of no effect, but in case of non-payment of the said sum at the time above mentioned with interest then the party of the second part may give to the party of the first part or the person in possession of the property and claiming the same written notice as required by law of his intention to foreclose this mortgage for breach of the condition thereof, and if the said sum is not then paid the party of the second part shall have full power and authority to enter upon the premises of the party of the first party or any other place or places where the aforesaid goods and chattels may be, to take possession of said property, to sell the same according to law, and the proceeds, after deducting all expenses of the sale and the keeping of the said property, to apply in payment of the above debt. If from any cause said property shall fail to satisfy the said debt, interest, costs, and charges, the party of the first part covenants and agrees to pay the deficiency.

In Witness Whereof I, the party of the first part, have hereunto set my hand and seal this *twentieth* day of *July, 1921.*

Sealed and delivered in the presence of
[*Signed*] T. B. Stinson

[*Signed*] Davis Coleman (seal)

State of Pennsylvania
County of Allegheny } *ss.:*

On *the twentieth* day of July, A. D., *one thousand nine hundred and twenty-one,* before me, the subscriber, a notary public of the Commonwealth of Pennsylvania, residing in the City of Pittsburgh, personally came the above-named *Davis Coleman,* who acknowledged the foregoing instrument to be his act and deed and desired that the same be recorded as such, according to law.

[*Signed*] William Buchanan,
Notary Public.

(notarial seal)

My commission expires January 10, 1923.

Fig. 2

42. A question often arises regarding the validity of a mortgage given by a merchant on his entire stock of merchandise. Suppose he remains in possession with a right to sell the goods in the usual course of trade, meanwhile keeping up the stock to a certain value. In Arkansas, the District of Columbia, Georgia, Indiana, Iowa, Kentucky, Maine, Maryland, Massachusetts, Michigan, Nebraska, New Jersey, North Carolina, North Dakota, Rhode Island, South Carolina, Utah, Vermont, Washington, and Wyoming it is held that where the mortgagor remains in possession with a power of disposal, the possession in itself is not fraudulent. Whether the transaction is a fraud on creditors and third parties is to be ascertained from all the circumstances of the case. Retention of possession by the mortgagor does not conclusively prove fraud. On the other hand, in Alabama, Colorado, Florida, Idaho, Illinois, Kansas, Minnesota, Mississippi, Missouri, Montana, New Hampshire, New Mexico, New York, Ohio, Oklahoma, Oregon, South Dakota, Tennessee, Texas, Virginia, and West Virginia it is held that the mortgagor's retention of possession with a power of disposal conclusively stamps the transaction as fraudulent.

43. In the case of very many chattel mortgages, the mortgagor is allowed to retain the goods in his custody. If the mortgagor fails to perform the condition of the mortgage, the mortgagee may take possession immediately after the default. If the mortgagee fails to gain possession within a reasonable time after default, he may find that other creditors have come in ahead of him against the property. When he has taken possession under a valid mortgage made in good faith, his rights may be maintained against the mortgagor and all other persons.

44. After the condition is broken the mortgagor has an equity of redemption similar to the right which exists in the case of real-estate mortgages. The value of the equity of redemption is usually the difference between the total value of the property and the mortgage debt. If the mortgagor desires to exercise his right to redeem, he must do so within a reasonable time. Fig. 2 is a form of chattel mortgage.

LEASES OF REAL PROPERTY

THE FORMATION OF THE RELATION OF LANDLORD AND TENANT

45. The principles involved in leases and sales of real property are somewhat similar to those relating to bailments and sales of personal property. For example, by virtue of a bailment, the bailee gets possession of personal property; by virtue of a sale of personalty he acquires the ownership of it. We may draw a similar distinction between leases of real property, which will now be considered, and sales of real property, which will be considered in Art. **63** and following. Under a lease, the lessee usually gets possession of the leased property, but not the ownership and title. When a valid sale of real property is made the purchaser gets title, but he may or may not go into immediate possession.

46. Certain long leases require special formality. A short contract of lease, however, usually may be made by conduct, by word of mouth, or by writing. These three methods of forming the relation of landlord and tenant will be considered in the order named.

(A) Contracts of lease implied from the conduct of the parties.

47. The rule that a contract need not be formed by written or spoken words, but may appear from the actions of the parties, applies in certain cases to the relation of landlord and tenant. In general, the owner of land may recover compensation from the person who has occupied it, where the situation is such that one may fairly infer an agreement on the latter's part to recognize the title of the owner. Sometimes, however, where a dependent occupies real estate belonging to a rich friend or relative, it would be unreasonable to allow a

recovery of rental in the absence of an express agreement to pay it.

STERRITT *v.* WRIGHT, 27 Pa. 259 (1856). For several years Peter Wright had the use of a farm belonging to his father-in-law, David Sterritt. After Wright had occupied the farm for four years, Sterritt sued him on an implied contract to pay rent. *Held* that Wright must pay a reasonable rent for the farm, unless he could prove that he was to occupy it gratuitously. This is based on the general principle that when one person receives anything of value from another the courts will imply a promise that he will pay what it is worth, unless the circumstances forbid them to draw such inference.

(B) Leases by word of mouth.

48. In most states the statutes of frauds require leases for more than a year to be in writing, although oral leases for a shorter period are usually binding. As a matter of business prudence, however, it is wise to put all leases in writing. See Part 2, Art. **74.** The ordinary printed or written forms of lease contain many terms which cannot be conveniently mentioned in a verbal agreement.

(C) Written or printed leases.

49. It makes no difference whether the terms of a lease are written or printed, for in either case they are presumed to express the intention of the parties. Where the lease is for a longer term than three years it is required in some states to be made by an instrument under seal. Both parties should sign the contract which should be executed in duplicate. The tenant should insist on receiving a copy of the lease, executed in precisely the same way as the copy which the lessor gets. The statutes of most states provide that leases exceeding a certain time shall be recorded in a designated local office in the county or district in which the land lies. Leases for more than one year must be recorded in California, Connecticut, Florida, Hawaii, Idaho, Montana, Nebraska, North Dakota, Oklahoma, South Carolina, South Dakota, and Vermont. Leases for more than two years must be recorded in Rhode Island. In Indiana, New York, North Carolina, Ohio, Tennessee, Wisconsin, and Wyoming, leases for more than three years must be recorded. In Kentucky, Virginia, and West

Virginia, leases for more than five years must be recorded. In Maine, Maryland, Massachusetts, and New Hampshire the

THIS INDENTURE, Made the *first* day of *September* in the year of our Lord, *one thousand nine hundred and twenty-one.*

BETWEEN *James Cleveland,* of *the City of Atlantic City, in the County of Atlantic and State of New Jersey,* of the first part, and *Lewis Betz,* of *the City of New York, in the County of Queens and State of New York,* of the second part.

WITNESSETH, that the party of the first part hath let, and by these presents doth grant, demise, and let unto the party of the second part *all that cottage dwelling house know as No. 3516 Pacific Avenue, in the City of Atlantic City, and State of New Jersey,* with the appurtenances, for the term of *one year* from this date, at the rent of *Ninety Dollars ($90) per month* to be paid in advance, on the first day of each and every month beginning the day of the date hereof.

PROVIDED, that if any rents shall be due and unpaid, or if default shall be made in any of the covenants herein contained, then it shall be lawful for the party of the first part, without notice and without any demand for the said rent, to reenter the said premises and remove all persons therefrom, or to proceed by action for the recovery of the possession thereof, or otherwise however.

AND the party of the second part doth hereby covenant and agree to and with the party of the first part, to pay the said yearly rent in the proportions and upon the conditions aforesaid; and not to underlet the said premises, or any part thereof, or to permit any person or persons to occupy the same, or any part thereof, or to use or permit any part thereof to be used for any other purpose than as a dwelling house, or to make or suffer to be made any alteration therein, without the written consent of the party of the first part; and also, at the expiration of the said term, to yield up and surrender possession thereof, with the appurtenances, in as good state and condition as the same now are in or may be put into by the party of the first part, reasonable wear and tear thereof and accidents happening by fire or other casualties excepted.

AND the party of first part doth covenant that the party of the second part, on paying the said rent, and performing the covenants aforesaid, shall and may, peaceably and quietly, have, hold, and enjoy the said demised premises for the term aforesaid.

IN WITNESS WHEREOF the said parties have interchangeably set their hands and seals hereto the day and year first above written.

Signed, sealed, and delivered in the presence of } [*Signed*] JAMES CLEVELAND (SEAL)

[*Signed*] JULIA JANSON } [*Signed*] LEWIS BETZ (SEAL)

FIG. 3

period is seven years. In Delaware and Pennsylvania leases for more than twenty-one years should be recorded.

A form of lease is shown in Fig. 3.

(D) Precautions to be observed by the tenant.

50. Where the buildings erected on leased premises are accidentally destroyed, as by fire, riot, tempest, or other cause, the tenant usually continues liable to pay rent, unless specially protected by the terms of the lease. Therefore, ordinarily he should insist upon the insertion of a clause in the lease providing that his liability for rent shall cease in case of the destruction of the buildings. See Arts. **49** and **61.**

EXCEPTION.—This rule does not apply where apartments in a building are leased without carrying any interest in the land. But in order to relieve the lessee of apartments of his liability to pay rent, it must appear not merely that they have been rendered untenantable by reason of fire or other casualty but also that they have been totally destroyed.

THE LANDLORD'S RIGHTS

51. The chief object that the landlord usually has in view is that of obtaining a return from the tenant for the use of the leased premises, called rent. Unless the lease provides otherwise or the custom of the place fixes a different time, rent is payable at the end of the term of the lease. Landlords, however, generally insert a provision in their leases that rent shall be payable in instalments on the first day of certain monthly, quarterly, or yearly periods. It is usual also to provide that rent shall be payable at whatever place the landlord may designate. Where the lease is silent on the subject, it is payable on the leased premises, and the landlord must go there for his money. If the rent is due and the tenant does not pay it, the landlord may sue for it, as in the case of every other broken contract. But he should first make demand for it on the premises, unless the agreement is that it shall be paid elsewhere.

(A) The right to distrain.

52. In addition to the landlord's right to sue for the rent, he has in most states the right to distrain. This right entitles the landlord, when the rent is in arrears, to enter the leased premises and sell tangible personal property found there to satisfy his claim. The general rule is that all goods and chat-

tels found on the leased premises, even those of a stranger, are subject to distress for rent. But there are many exceptions to this rule, and the tendency is to restrict the landlord's right to distrain. In Alabama, the District of Columbia, Georgia, Louisiana, Massachusetts, Minnesota, Mississippi, Missouri, Montana, New York, North Carolina, Utah, and Wisconsin, the right of distress does not exist.

(B) Where the tenant holds over.

53. Most leases provide that if neither the tenant nor the landlord gives certain notice of an intention to terminate the lease, it shall be extended for a further named period. If the tenant holds over under this clause, he is held to be subject to all the conditions of the lease which are applicable to the renewed tenancy. Where the agreement of lease contains no provision for holding over, the landlord usually has the option of treating a tenant who remains in possession either as a tenant for a full year by reason of his holding over, or as a trespasser. If the landlord duly notifies his tenant of an intention to terminate the lease, the tenant who holds over after the expiration of his term becomes a trespasser.

54. Upon the expiration of a lease, it is the tenant's duty to vacate the premises. Therefore, he should be careful to move out on time. Holding over by a subtenant after the expiration of the term has the same effect as a holding over by the main tenant, and the landlord, therefore, usually may hold the latter for another year.

(C) The tenant's duty of loyalty.

55. The tenant owes a certain duty of loyalty to his landlord. This duty precludes him while in possession of leased premises from denying the title of his landlord. But while he is forbidden to assert that his landlord never had any title, he may prove that, since he became a tenant, the landlord has ceased to hold title.

THE TENANT'S RIGHTS

(A) The condition of the premises.

56. Usually the tenant has no right to demand of his landlord that the leased premises shall be in fit condition for the purposes for which they are rented, unless the landlord has agreed to put them in such condition. The lessee takes the risk, and he should examine the premises he intends to lease, and determine from his own inspection whether or not they are suitable for his purpose.

FRIEDMAN *v.* SCHWABACKER, 64 Ill. App. 422 (1896). H. and J. Schwabacker rented a store and basement from Samuel Friedman. The Schwabackers defended an action by Friedman for rent on the ground that the leased premises were in such a filthy and unsanitary condition as to be untenantable. *Held,* that Schwabackers were liable for the rent. Although they had not inspected the premises before leasing them, they signed a lease wherein they stated that they received the premises in good repair and agreed to keep them in repair at their own expense. There was no implied contract on the part of Friedman that the leased premises were tenantable or that they would continue to be so during the term. The Schwabackers took the premises as they found them, and had to hold them subject to the provisions of their lease.

57. But where there are concealed defects in the leased premises which may be dangerous to the tenant and which are known to the landlord, he may be liable if he does not disclose such defects to the tenant and injury results to the tenant by reason thereof.

(B) The right to peaceful occupancy.

58. In most leases, in the absence of a special provision to the contrary, a covenant or promise will be implied on the landlord's part that the tenant shall have quiet and uninterrupted enjoyment of the premises undisturbed by the landlord himself or by any one having a better title than the landlord.

59. The tenant's right to quiet enjoyment is clearly infringed if he is put out of possession of the leased premises. And in general, anything of a grave and permanent character done by the landlord with the intention of depriving the tenant

of the enjoyment of the leased premises will be regarded as an invasion of the tenant's rights.

(C) As regards repairs.

60. Unless the landlord has expressly contracted to make repairs on the leased premises, the tenant cannot compel him to do so. Therefore, in the absence of any express agreement, the tenant cannot make repairs at his own expense and either charge them to the landlord or deduct their cost from the rent. Where the landlord voluntarily makes repairs, the law will not imply a contract on his part to continue doing so.

61. It is generally considered the tenant's duty to make ordinary repairs. Most leases, therefore, contain a covenant on the part of the lessee to repair, whereby he is bound to deliver up the premises at the end of the term in as good order and condition, reasonable use and unavoidable casualties excepted, as when received from the lessor. The tenant should be careful about the wording of a covenant of this character which is inserted in his lease. If he binds himself to repair, he may find in case of the total destruction of the building by fire, tempest, or any other cause than the act of the landlord, that he has obligated himself to rebuild. If the lease binds the tenant "to return and redeliver the house at the end of the term, in good order and condition, reasonable wear and tear only excepted," he would have to rebuild in case of the destruction of the property by fire. Hence, it is desirable, from a tenant's viewpoint, to have the lease provide that, in case of the destruction of the leased building through fire or other casualty, he shall be under no liability to pay further rent or to restore the premises to their former condition.

(D) To remove fixtures and other improvements.

62. Fixtures are defined as personal chattels which have been attached or affixed to real estate by a tenant. In most states fixtures put in by a tenant are removable by him, provided he does so while lawfully in possession of the leased premises. As a rule he may remove trade, ornamental, and domestic fixtures, if he can do so without injuring the premises.

SALES AND MORTGAGES OF REAL PROPERTY

CONTRACTS TO SELL AND CONVEYANCES OF REALTY

63. In sales of real estate two documents are usually prepared and executed. The first is the agreement to sell, and the second is a conveyance in performance of the agreement. The conveyance carries out the agreement of sale, and transfers the legal title to the purchaser. The transfer usually takes place at the moment when the deed is delivered to the purchaser.

(A) The formation of a contract to sell realty.

64. The statutes of the various states require a contract for the sale of realty, or of any interest therein, to be in writing, and signed by the seller or his agent. See Part 2, Art. **73.** Such contract is not a conveyance of the land, but merely an agreement to convey it at some future time. If the buyer believes that the seller is likely to disregard the contract and convey the property to some third party, he may protect himself by having the contract of sale recorded. If the contract is to be recorded, it should be acknowledged by the seller before a notary public or some other proper official.

65. After a party has agreed to buy land, the next step is for him to assure himself that the seller has a good title. He must not only make sure that the person who has agreed to sell really owns the property, but also that no third parties have any claims or liens against the property by means of judgments against the owner or otherwise. This is done by having a lawyer, a conveyancer, or a title company search the records in the public offices where deeds, mortgages, and certain other important documents pertaining to real estate are recorded,

and prepare an abstract or brief of title and a certificate of search showing all such matters so far as they affect the property. This abstract will inform the purchaser of any defects in the way of the seller's conveying a perfect title. Usually the buyer may refuse to perform the contract if the search shows that the seller cannot give him a good and marketable title. Generally it is wise for him, if possible, to have the title insured by a company which issues insurance policies of this kind.

(B) The performance of a contract to sell realty by executing and delivering the deed and making settlement.

66. When the parties are ready to perform the contract, the purchaser should see that the formalities of signing, sealing, attestation, acknowledgment, and delivery are complied with, and, where United States revenue stamps are necessary, that these are affixed in the proper amounts.

67. It is a general requisite to the validity of deeds conveying real estate that they shall be signed by the party making them or his duly authorized agent. If the grantor is unable to write, he may sign by "making his mark." Where the deed is executed by an agent, his authority should be evidenced by an instrument of equal dignity with that which he is authorized to execute. Hence, a power of attorney to execute a deed should be signed, sealed, and acknowledged with the same formality as the deed of conveyance itself. Deeds made by a corporation should be signed in the corporate name by the president or some other proper official, and the corporate seal should be affixed and attested by the secretary or some other designated officer.

68. In most states a seal is necessary to render valid even a private person's deed. Strictly speaking, a seal is an impression on wax or other tenacious substance. Now the word "seal," the letters "L. S.," or even a mark will usually be recognized as a seal if it is clear that a party intended to adopt it as his seal. In some states the distinction between sealed and unsealed instruments has been abolished, the modern ten-

dency being to dispense with the use of the seal as much as possible. But while in some states it is not necessary that a deed shall be sealed by the party making it, no harm will be done by having the grantor's seal affixed. See Part 1, Arts. **58** and **61.**

69. Generally, in order that a deed may be recorded, it is necessary that it be attested by one or more witnesses. No person having a direct interest in the conveyance should be an attesting witness to it. In addition to the common requirement of attestation, it is usually necessary that the grantor shall acknowledge the instrument. Acknowledgment is the declaration before a notary public or some other competent official by one who has executed an instrument that it is his act and deed.

70. After a deed has been duly signed, sealed, attested, and acknowledged, the next formality is that of delivery. The deed operates to transfer title only when it is delivered to the grantee. When a deed is handed to a third party to be delivered to the grantee upon the performance of a certain condition, it is said to be delivered in escrow. The title then passes on the performance of the condition and the delivery of the deed to the grantee by the third party. Ordinarily delivery to the grantee is made when he pays for the property or gives security for payment. This is called "the settlement," and marks the fulfilment of the contract of sale.

71. If the premises to be conveyed are occupied by a tenant, the purchaser is bound to take notice that they are held subject to the terms of the agreement of lease. An agreement of sale usually provides that rent shall be apportioned between the seller and the buyer as of the date of settlement.

(C) The necessity of recording.

72. Statutory provision is made in every state for the registration or recording in a designated local office of deeds, mortgages, and certain other documents concerning land. The effect of the recording of instruments which are entitled to be recorded is to give the whole world legal notice of their exis-

tence. Every one is bound to know that the deed or other instrument is on record, even though he has no actual knowledge of the fact. Failure to record a deed or mortgage does not affect its validity as between the immediate parties. If the grantee does not record his deed, it is void as against any one who subsequently purchases the same property in good faith, and who has had no means of learning about the previous conveyance.

RIGHTS AND OBLIGATIONS OF THE PARTIES TO A SALE OF REALTY AFTER TITLE HAS PASSED

(A) Obligations of the seller toward the buyer.

73. The obligations of the seller of real property toward the buyer after title has passed depend upon the nature of the deed of conveyance. Broadly speaking, there are two kinds of deeds; (1) the quit-claim deed and (2) the warranty deed.

1. Quit-Claim Deeds

74. By a quit-claim deed the seller does not represent to the buyer that he has any title whatever, but merely conveys to the buyer any "right, title, or interest" which he may have in the premises. If it turns out that the seller had a defective title, the buyer seldom has any right of action against him. Sometimes the seller inserts in a quit-claim deed a covenant of special warranty, by which he represents to the buyer that he has not himself done or knowingly permitted to be done anything which would injure his title to the property.

75. A form of quit-claim deed is shown in Fig. 4.

2. Warranty Deeds

76. In a warranty deed the seller may make any one or all of the following four covenants: (1) of seisin and of his right to convey; (2) that the real estate is free from encumbrances; (3) of peaceable enjoyment; (4) for further assurances.

77. Usually the first covenant in a warranty deed is that of seisin and of the right to convey, whereby the seller represents to the buyer that he has title to the premises which he

THIS INDENTURE, made the *fifteenth* day of *September* in the year *one thousand nine hundred and twenty-one.*

BETWEEN *Henry W. Middleton and Sarah Jane, his wife, of the City of Camden, in the County of Camden, and State of New Jersey,* parties of the first part, and *Albert Waterman, of the same place,* party of the second part,

WITNESSETH that the parties of the first part, in consideration of the sum of one dollar, lawful money of the United States, paid to them by the party of the second part, do hereby remise, release, and forever quit-claim unto the party of the second part, his heirs and assigns forever,

ALL *that certain messuage or tenement and lot or piece of ground situate on the east side of Ninth Street at the distance of one hundred and ninety-eight feet northward from the north side of Atlantic Avenue in the City of Atlantic, County of Atlantic, and State of New Jersey, being part of Lot No. 19 in the said City, bounded and described as follows, to wit: Beginning at the east corner of land now or late of Isaac W. Kaighn and running thence north twenty-eight feet and one-half of a foot; thence east to the east line of Lot No. 19; thence south to land now or late of Joseph C. Armitt; thence south to the center of the said Ninth Street and thence west to the place of beginning.*

TOGETHER with the appurtenances and all the estates and rights of the parties of the first part in the said premises, to have and to hold the above described premises unto the party of the second part, his heirs and assigns forever.

IN WITNESS WHEREOF the parties of the first part have set their hands and seals hereto the day and year first above written.

Signed, sealed, and delivered in the presence of [*Signed*] FRANCIS X. HALL

[*Signed*] HENRY W. MIDDLETON (SEAL)
[*Signed*] SARAH JANE MIDDLETON (SEAL)

STATE OF NEW JERSEY
ATLANTIC COUNTY } *ss.:*

BE IT REMEMBERED, That on this *fifteenth* day of *September,* in the year of our Lord *one thousand nine hundred and twenty-one,* before me, a Commissioner of Deeds, personally appeared *Henry W. Middleton and Sarah Jane, his wife,* who I am satisfied are the grantors named in the foregoing Deed of Conveyance, and, I having first made known to them the contents thereof, they acknowledged that they signed, sealed, and delivered the same as their voluntary act and deed; and the said *Sarah Jane Middleton,* being of full age, on a private examination apart from her said husband, before me acknowledged that she signed, sealed, and delivered the same as her voluntary act and deed, freely, without any fear, threats, or compulsion of her said husband. All of which is hereby certified.

{COMMISSIONER'S OFFICIAL SEAL}

[*Signed*] ADOLPH T. CASEY

FIG. 4

undertakes to sell. This covenant is satisfied if the seller is in lawful possession of the premises either by himself or by another. It would be broken, however, if the seller should undertake to convey the entire property while owning merely one-half of it.

78. The second covenant is that against encumbrances, whereby the seller represents to the buyer that no rights in or to the land conveyed, which would lessen the value of the property, are held by mortgagees, judgment creditors, or other lien claimants. This covenant would be broken if it should appear after the delivery of the deed that there was an outstanding mortgage against the property.

79. The third covenant is that of peaceable enjoyment by which the seller agrees with the buyer that the buyer shall not be disturbed in his enjoyment of the property. By a general warranty the seller undertakes that the buyer shall not be disturbed by any person whomsoever. By a special warranty he undertakes to protect the buyer merely against particular persons, generally against the seller himself or any one claiming under him.

80. The fourth covenant is that for further assurances, whereby the seller agrees to perform such further acts and to procure such further documents as may be necessary to remove any defects subsequently appearing in the buyer's title.

81. In the case of a breach of any of these covenants, the buyer has the right to hold the seller for whatever damages he may suffer by reason of such breach. In Fig. 5 is shown a form of deed containing the four covenants set forth, with a clause of general warranty.

(B) Obligations of the buyer toward the seller.

82. In many cases when property it conveyed, it is sold "subject" to an existing mortgage. This does not have the effect of making the purchaser of the property personally liable for the amount of the mortgage debt, unless he expressly assumes such liability. The land is the security for the payment of the debt, and the purchaser is bound to recognize the

THIS INDENTURE, Made the *twenty-seventh* day of *October* in *the year one thousand nine hundred and twenty-one.*

BETWEEN *Henry Wood,* of *West Point, Orange County, New York,* party of the first part, and *John J. Wurts,* of *Freehold, Green County, New York,* party of the second part,

WITNESSETH that the party of the first part in consideration of the sum of *Six Thousand Five Hundred Dollars* (*$6,500*), lawful money of the United States, paid by the party of the second part, does hereby grant and release unto the party of the second part, his heirs and assigns forever,

ALL *that tract or parcel of land situate in the City of Albany, County of Albany and State of New York, situate on the easterly side of Pemberton Street at the distance of one hundred and twenty-eight feet northward from the northerly side of Master Street containing in front or breadth on Pemberton Street eighteen feet and extending of that width in length or depth eastwardly between lines parallel with said Master Street twenty-seven feet and four inches,*

TOGETHER with the appurtenances and all the estate and rights of the party of the first part in and to the said premises,

TO HAVE AND TO HOLD the above granted premises unto the party of the second part, his heirs and assigns forever.

AND the said *Henry Wood,* party of the first part, covenants with the said *John J. Wurts,* party of the second part, as follows:

FIRST. That the party of the first part is seized of the said premises in fee simple and has a good right to convey them.

SECOND. That the said premises are free from encumbrances.

THIRD. That the party of the first part will forever warrant and defend the title of the party of the second part to the said premises against all and every person or persons whomsoever lawfully claiming or to claim the same or any part thereof.

FOURTH. That the party of the first part will execute or procure any further necessary assurance of the title to the said premises.

IN WITNESS WHEREOF the party of the first part has set his hand and seal hereto the day and year first above written.

[*Signed*] HENRY WOOD (SEAL)

Sealed and delivered in the presence of
[*Signed*] JAMES A. REED
[*Signed*] GEORGE S. BRYANT

$6.50 in U. S. revenue stamps, cancelled

CITY OF NEW YORK
COUNTY OF KINGS } *ss.:*
STATE OF NEW YORK.

This *twenty-seventh* day of *October* in the year *nineteen hundred and twenty-one,* before me, the subscriber, personally appeared *Henry Wood,* to me personally known to be the same person described in and who executed the foregoing instrument, who acknowledged to me that he executed the same.

[*Signed*] HOWARD THOMPSON,
(NOTARIAL SEAL) Notary Public of Kings County, N. Y.

FIG. 5

mortgage as a valid charge against the land. The purchaser gets merely the equity of redemption, the difference between the value of the property and the amount of the mortgage debt. After he transfers the property to a third party, he is no longer interested in its payment. Usually, however, the person who originally made the mortgage remains liable on the note or the bond to secure which the mortgage was given.

83. Until the seller's deed is delivered he retains a lien on the real estate for the purchase money, unless he expressly waives it. This rule is similar to the one concerning the sale of personalty, namely, that the seller before delivering possession of the personalty usually retains a lien on it for the purchase money. The delivery of the deed, which represents the title and ownership, roughly corresponds to the manual delivery of tangible articles of personal property.

MORTGAGES OF REALTY

84. A mortgage is a conveyance of land as security for the performance of an obligation, generally the payment of a debt, with a provision that the conveyance shall be void upon the performance of the obligation. The person who gives the mortgage is called the mortgagor, and the person to whom it is given is called the mortgagee. In general, any interest in real property which may be sold may also be mortgaged. While mortgages have to do with interests in land, the mortgages themselves are personal property.

85. The usual form of mortgage is similar to an ordinary deed of conveyance with the addition of a clause of defeasance. This clause provides that the conveyance shall be void upon the performance of certain conditions, generally the payment of the mortgage debt. Mortgages are usually executed with the same formality that is required in the case of deeds.

(A) Obligations of the mortgagor toward the mortgagee.

86. It is the mortgagor's duty to pay the interest due under the terms of the mortgage upon the day specified, together with

taxes and other assessments which may be imposed upon the property. The mortgagor has an insurable interest in the premises, and in many cases he is obliged, under the terms of the mortgage, to keep the buildings insured against fire for the benefit of the mortgagee to the amount of the mortgage debt.

87. For a breach of any of the conditions of the mortgage, such as a failure to pay the interest, the taxes, or other charges against the property within a certain time after they fall due, or the failure to pay the mortgage debt at maturity, the mortgagee has the right to foreclose. Foreclosure is the means whereby the mortgagee applies the mortgaged premises, which have been conveyed as security, to the payment of his debt. The usual form is a legal proceeding by which the property is sold and the proceeds applied to the liquidation of the debt. If anything remains after the mortgagee has been paid the debt, with interest and legal costs, this surplus is turned over to the mortgagor.

(B) Obligations of the mortgagee toward the mortgagor.

88. Ordinarily the mortgagor may remain in possession of the premises until he has broken some condition of the mortgage and it has been foreclosed. But if the mortgagee goes into possession of the mortgaged premises before breach of condition by the mortgagor, he is obliged, upon payment of the mortgage or upon the termination of the foreclosure proceedings, to account to the mortgagor for the rents and profits of the land. Ordinarily he should apply them to the reduction of the mortgage debt. If the mortgagee does not manage the mortgaged premises carefully, but incurs loss by reason of renting them to a notoriously bad tenant, he may be liable to the mortgagor for the fair rental value of the property. A mortgagee who occupies the property himself must pay the mortgagor its fair rental value or credit him therewith on account of the mortgage debt.

89. When the mortgagee forecloses on account of the mortgagor's non-performance of some specified condition, the

property is sold and the proceeds are applied to the satisfaction of the mortgage debt. When the foreclosure proceeding is carried out to a conclusion, the mortgagor loses all his title and right in the property.

90. A mortgage will be discharged by the mortgagor's performance of all the specified obligations, usually the payment of the mortgage debt with interest. When such performance has been completed, the mortgage should be satisfied of record in the public office wherein it was recorded originally.

A form of mortgage is shown hereafter. As indicated therein, it is security for the payment of a bond or a note. The bond or the note is deemed the primary instrument to which the mortgage is auxiliary. No form of bond or note is here shown: the form varies widely in the various states.

Form of Mortgage

This Indenture, made the *twentieth* day of *July, one thousand nine hundred and twenty-one.*

Between *William Carr, teamster, single man,* of *the City of Newark, County of Essex and State of New Jersey,* party of the first part, and *George Moffat, banker,* of *the same place,* party of the second part,

Whereas the party of the first part in and by his obligation or writing obligatory under his hand and seal duly executed bearing even date herewith, stands firmly bound to the party of the second part in the sum of *Six Thousand Dollars* (*$6,000*), lawful money of the United States of America, conditioned for the payment of the just sum of *Three Thousand Dollars,* lawful money as aforesaid, at the expiration of *five* years from the date hereof, together with interest thereon, payable semiannually at the rate of *six* per cent. per annum, without any fraud or further delay,

NOW this indenture witnesseth that the party of the first part as well for and in consideration of the aforesaid sum of *Three Thousand Dollars* and for the better securing the payment of the same with interest as aforesaid, unto the party of the second part, his executors, administrators, and assigns and also for and in consideration of the further sum of one dollar unto him in hand well and truly paid by the party of the second part at and before the ensealing hereof, the receipt whereof is hereby acknowledged, does by these presents grant and release unto the party of the second part, his heirs and assigns forever,

All *that tract or parcel of land, situate in the City of Camden, in the County of Camden and State of New Jersey, bounded and described as follows: Beginning at a point in the northerly edge of Pacific Street, distant one hundred feet easterly from the northeasterly corner of Fourth and Pacific Streets, thence* (1) *northwardly parallel with Fourth Street one hundred and fifty*

feet to the line of lot No. 13; *thence* (2) *eastwardly parallel with Pacific Street thirty-one feet; thence* (3) *southwardly parallel with Fourth Street one hundred and fifty feet to the northerly edge of Pacific Street; thence* (4) *westwardly along and in the said northerly edge of Pacific Street thirty-one feet to the place of beginning.*

Together with the appurtenances, and all the estate and rights of the party of the first part in and to said premises.

To Have and to Hold the above-granted premises unto the party of the second part, his heirs and assigns forever.

Provided Always, nevertheless, that if the party of the first part, his heirs, executors, administrators, or assigns do and shall well and truly pay or cause to be paid unto the party of the second part, his heirs, executors, administrators, or assigns, the aforesaid principal sum of *Three Thousand Dollars* on the day and time hereinbefore mentioned and appointed for payment of the same together with interest as aforesaid, then and from thenceforth as well this present indenture and the estate hereby granted as the said recited obligation shall cease, determine and become void, anything hereinbefore contained to the contrary notwithstanding.

And the party of the first part covenants with the party of the second part as follows:

That the party of first part will pay the indebtedness as hereinbefore provided, and if default be made in payment as aforesaid, the party of the second part shall have power to sell the premises herein described, according to law.

In Witness Whereof, the party of the first part has set his hand and seal hereto the day and year first above written.

In the presence of
[*Signed*] James Casey

[*Signed*] William Carr (seal)

State of New Jersey
County of Camden } *ss.:*

On this twentieth day of July, in the year one thousand nine hundred and twenty-one, before me, the subscriber, personally appeared William Carr, to me personally known to be the same person described in and who executed the foregoing instrument, and he acknowledged to me that he executed the same.

[*Signed*] Charles A. Hogan,
Commissioner of Deeds in and for the State of New Jersey

[seal of commissioner of deeds]

My commission expires February 2, 1923.

AMERICAN BUSINESS LAW
(PART 9)

SURETYSHIP AND GUARANTY

THE NATURE AND THE FORMATION OF SURETYSHIP AND GUARANTY CONTRACTS

(A) Nature of the contract.

1. A contract of suretyship is defined as an agreement whereby one person engages to be answerable for the debt, default, or miscarriage of another. A contract of guaranty is defined as a promise to answer for some debt or the performance of some other obligation in case the person who is first liable to pay or perform cannot do so.

1. Such Contracts Distinguished From Original Undertakings

2. An original undertaking must be distinguished from a contract of suretyship or guaranty. One entering into an original undertaking assumes liability for the performance of his own part of the transaction, while a contract of suretyship or guaranty is an agreement to answer for the debt or default of another. The original undertaking involves a primary liability; the contract of suretyship or guaranty involves only a secondary liability depending upon the default of another who is primarily liable.

Dickinson *v.* Colter, 45 Ind. 445 (1874). Dickinson signed and delivered to Colter a written agreement, which, after reciting that Colter was about to appoint Berry his agent for the sale of grain and to furnish

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Berry with money for that purpose, continued: "I hereby become responsible to said Colter and agree to pay him all money that he may advance to said Berry and that may be due him from Berry from time to time by reason of such advances." *Held* that Dickinson's liability was original, primary, and absolute. He unconditionally agreed to pay Colter all moneys which the latter might advance to Berry.

Dole *v.* Young, 24 Pick. (Mass.) 251 (1837). The following writing was signed and addressed to Dole by Young: "Please send Amos Wetherbee goods to the amount of $100 and I will guarantee the same in four months." Immediately after the presentation of the writing Dole delivered goods to Wetherbee. This suit was brought to recover the price of the goods from Young. *Held* that Young was liable. The writing was not an original undertaking, but a collateral agreement to pay in case Wetherbee should not do so. It was, therefore, a contract of guaranty of Wetherbee's debt.

2. Suretyship Distinguished From Guaranty

3. A suretyship obligation is a direct liability assumed by a third person to the obligee for the act to be performed by the principal obligor, while a guaranty creates a liability only for the principal's ability to perform the act. The contract of suretyship puts the surety under an immediate obligation that the act shall be done. The contract of guaranty is a separate contract in the nature of a warranty that the principal obligor is able to perform. Thus, a debtor's surety undertakes to pay if the debtor does not, while a guarantor undertakes to pay if the debtor cannot. The surety insures payment of the debt, while the guarantor is an insurer of the debtor's solvency.

(B) Formation of the contract.

1. Offer and Acceptance

4. This first contractual element is treated at length in Part 1, Arts. **25-27.** The general rule is that an offer to become surety or guarantor must be accepted before a contract of suretyship or guaranty is formed. But in this, as in other contracts, the nature of the undertaking and the situation of the parties should be borne in mind. Where the offer of guaranty is based upon a mere letter of credit, and the guarantor has no means of knowing whether or not his offer has been accepted and the extent of his liability, mere acting upon

the offer is not a sufficient acceptance. The guarantor must be notified within a reasonable time. But where the guaranty is for the payment of a preexisting debt or for the performance of any other contract already made, and is entered into on account of a new consideration passing from the creditor to the guarantor, direct notice of acceptance is not ordinarily necessary. Acting on the offer is usually sufficient acceptance, although it is wise to give explicit written notice of the acceptance.

WRIGHT *v.* GRIFFITH, 121 Ind. 478 (1889). Mrs. W. E. Headington applied to Griffith to purchase merchandise on credit. He refused, but when her father, Wright, wrote Griffith as follows, "I will stand good for the money to settle her bills," Griffith furnished her the merchandise requested. In a suit to recover the purchase price, the defense was that Wright had not been notified of Griffith's acceptance of his offer. *Held* that Wright was liable. His letter was not a mere overture, but the final consummation of a pending arrangement, in pursuance of which Griffith furnished Mrs. Headington with merchandise. When the guaranty is executed contemporaneously with, and as a part of the consideration for, the contract guaranteed, no notice of the acceptance of the guaranty is required.

2. SEAL AND CONSIDERATION

5. This topic is treated in Part 1, Arts. **58-77.** Alike with all other contracts, contracts of suretyship and guaranty must be under seal or supported by a consideration. Consideration may consist of some advantage to the principal obligor or the surety, or some disadvantage to the obligee. It is advisable to have a suretyship or guaranty contract under seal, lest a question be raised as to the consideration sustaining the surety's or guarantor's promise. But see Part 1, Art. **61.**

3. CAPACITY OF PARTIES

6. This topic is treated generally in Part 2, Arts. **1-27.** The suretyship and guaranty contracts of a minor are, like his other contracts, voidable by him at his option when he reaches full age. If an insane or intoxicated person enters into a contract of suretyship or guaranty, the agreement is seldom binding upon him. In states where all the disability of coverture has been removed, a married woman may make a contract of

suretyship or guaranty just as if she were single. In most states, however, her power to make contracts of this kind is restricted by statute; by denying her the power, either altogether or else merely in a particular case, as, for example, where she is not allowed to become surety or guarantor for her husband.

4. Reality of Consent

7. The contract of suretyship or guaranty involves the utmost good faith. When a man undertakes to go security he has a right to expect the fairest treatment. If he is deceived by any material misrepresentation or any improper concealment substantially affecting the transaction, and the obligee knows of such misrepresentation or concealment, the obligee cannot hold the surety or guarantor. See Part 2, Art. **37.**

Frank Fehr Brewing Co. *v.* Millican, *et al.*, 66 S. W. (Ky.) 627 (1902). Frank Fehr Brewing Company contracted with L. T. Millican to furnish beer at a stipulated price. Millican was to pay for all beer sold within thirty days after delivery. J. S. Millican and J. A. Lyddane were his sureties for the faithful performance of his contract. After the contract had run about four months, Lyddane inquired of the brewing company as to the standing of L. T. Millican's accounts. The brewing company replied that everything was "O. K.—that Millican owed only $400." In fact he was months behind in his payments and owed over $1,600. When Millican failed the company sued his two sureties. *Held* that the company could not recover. The fact that L. T. Millican had fallen behind in his accounts was of material importance. The brewing company's failure to reveal it when asked for information was a violation of good faith and vitiated the contract.

5. Legality of Object

8. If the undertaking of the principal is void, because it has an illegal object, the surety's or guarantor's undertaking is equally void. See Part 2, Arts. **49-70.**

6. Special Formality

9. A contract to answer for another's debt or default should be in writing and signed by the party who is to be charged or by his authorized agent. See Part 2, Art. **81.** A verbal contract of suretyship or guaranty is usually unenforceable. Of course, the requirement that the contract be in writing does

not dispense with the necessity of a consideration, unless the instrument is under seal, and of the other elements required in all contracts.

7. Authority of Agents and Partners

10. A person may make a contract of suretyship or guaranty through his authorized agent. But a creditor before accepting such contract, signed by an agent who assumes to bind his principal, should make certain that the agent is duly authorized. The agent's authority, however, need not be in writing.

11. The authority of a partner to bind the firm extends only to matters which are within the scope of the firm business. Therefore, the agency of one partner for the firm does not permit him to enter into contracts of suretyship and guaranty on behalf of the firm unless this is in the regular course of the firm's affairs, or unless he has been specially authorized to do so by his fellow partners.

RIGHTS AND OBLIGATIONS OF THE PARTIES

(A) Duties of the obligee toward the surety or the guarantor.

1. To Take Action Against the Principal

12. A surety is directly and immediately liable to the obligee. It is, therefore, not necessary for the obligee to proceed against the principal obligor or to realize on collateral security before he can hold the surety liable, unless the terms of the contract expressly require him to proceed first against the principal or against the collateral security given by the principal.

King & Houston *v.* State Bank, 9 Ark. 185 (1848). Stephenson made his note to the State Bank. King and Houston were his sureties. In an action against King & Houston, their defense was that the bank had neglected to sue Stephenson until after he became insolvent. *Held,* they were nevertheless liable. The creditor's forbearance did not violate any of the rights of the sureties and was not a good ground of defense.

13. In many states, if a surety thinks he is in danger and notifies the obligee to proceed against the principal obligor, and the obligee disregards the notice, the surety will not be discharged, even though at the time of the notice the principal was solvent so that the obligee could have obtained his money by obeying the notice.

14. In Alabama, Arkansas, California, Colorado, Georgia, Illinois, Indiana, Kentucky, Mississippi, Missouri, New York, North Carolina, Oklahoma, Pennsylvania, Tennessee, Texas, Virginia, Washington and West Virginia, if the surety fears that the principal is about to become insolvent or remove from the state without fulfilling the contract, he may demand that the obligee bring suit, declaring that unless this is done the surety's liability will cease. If the obligee fails to sue, the surety may be discharged.

MARTIN v. SKEHAN, 2 Colo. 614 (1875). Patrick Skehan was surety for the payment by Pierce Skehan of a promissory note held by Martin. Martin sued Patrick Skehan as surety. *Held*, as Patrick had requested Martin to proceed against the principal who was then solvent, he was exonerated by Martin's failure to do so, the principal afterwards having become insolvent.

15. When the contract is one of guaranty, usually the guarantor's liability does not arise merely upon the principal obligor's non-performance. Reference should always be had to the contract between the parties to ascertain what steps the obligee must take in order to fix the guarantor's liability. It may provide that the obligee shall pursue the principal obligor with diligence, and on failure to enforce performance inform the guarantor of such failure.

16. When the guaranty is conditional and the guarantor undertakes to indemnify the obligee against loss by reason of failure to collect a debt, the obligee must exercise reasonable diligence in pursuing the principal to obtain payment. But if it is evident that legal proceedings against the principal would be useless by reason of his insolvency, usually the obligee need do no more than make demand for payment upon the principal,

and, on being refused, he may then proceed against the guarantor.

DILLMAN *v.* NADELHOFFER, 160 Ill. 121 (1896). Edward Knowlton made his promissory note to the order of John Nadelhoffer. Before it was delivered to Nadelhoffer, Lewis E. Dillman indorsed it as follows: "I guarantee the collection of the within note. LEWIS E. DILLMAN." Knowlton did not pay at maturity and Nadelhoffer sued him. Before he obtained judgment Knowlton became insolvent. Then Nadelhoffer sued Dillman, the guarantor. *Held* that Nadelhoffer could recover. Dillman's undertaking was to pay the debt on condition that Nadelhoffer should use the ordinary legal means to collect it from Knowlton diligently but without success. The insolvency of the principal debtor, Knowlton, excused Nadelhoffer's failure to prosecute the suit to judgment.

17. Where the contract is one of absolute guaranty, the guarantor is in most states liable immediately upon the principal's non-fulfilment of his obligation. No further steps, such as pursuit of the principal obligor or proof of his insolvency, are necessary to fix the guarantor's liability. Guaranty without the imposition of conditions is sometimes held to be an absolute undertaking.

WINCHELL *v.* DOTY, 15 Hun (N. Y.) 1 (1876). Doty, on buying a horse from Winchell, offered in part payment a note made by Cartwright & Hoover, then four years past due. Winchell refused to accept it until finally Doty wrote on the back of it, "I guarantee the within note," and signed it. *Held,* this was a guarantee that payment would be promptly made and not merely that the note was collectible. It was an absolute undertaking and Winchell could sue and recover from Doty without first demanding payment of Cartwright & Hoover.

2. To Give Notice of the Principal's Default

18. From the nature of his obligation, a surety is not usually entitled to notice of the principal obligor's default. The surety has undertaken to become bound as the principal is bound, and accordingly the only thing the creditor need do in order to recover from the surety is to show that the principal has failed to fulfil his obligation.

BUCHANAN COUNTY *v.* KIRTLEY, 42 Mo. 534 (1868). Hugh Irwin contracted to build a bridge for Buchanan County and warranted the bridge to stand for four years. Kirtley was his surety. Within the time named, the bridge became entirely unfit and unsafe. The county had the necessary repairs made and sued Kirtley to recover the cost.

Held that Kirtley was liable. No written notice was required to be given to him to hold him responsible on his obligation. He was required to take notice of any breach that should occur and repair the same in conformity with his contract.

19. In a guaranty contract, whether or not notice is required depends upon the nature of the transaction. The contract itself may require notice. Or the circumstances may be such that the principal's default, while known to the party to whom the guarantor is liable, would not naturally be known to the guarantor. In such cases notice should be given. If a guaranty is conditional, failure to give the guarantor notice within a reasonable time of the principal debtor's default generally entitles the guarantor to defend an action on the guaranty to the extent that he has suffered damage by the omission. In an absolute guaranty, the guarantor's liability is coextensive with that of the principal debtor. Therefore, in such cases, proof of notice of the principal's default is not necessary to fix the guarantor's liability.

Reeves *v.* Howe, *et al.*, 16 Cal. 152 (1860). Hayward wrote on the back of a note drawn by Howe and Mayo and payable to Reeves or order: "I guarantee the collection of the within note when due. (Signed) A. Hayward." The note not being paid, Reeves sued Hayward as guarantor. *Held* that Hayward was entitled to legal notice of non-payment before he could be held on his contract. His agreement was not original but collateral, and was a mere conditional promise to pay if the makers should not. He was entitled to notice of the principal debtors' default.

Rogers *v.* Burr, 97 Ga. 10 (1895). Burr was induced to subscribe for stock in the Barnesville Manufacturing Company upon the faith of a written agreement signed by Rogers, guaranteeing an 8 per cent. dividend on the stock for a period of three years. She sued Rogers to recover the dividend. His defense was that she had never notified him of the company's failure to pay dividends. *Held* that the guaranty was absolute and unconditional, and no notice to the guarantor of his principal's default was required. It was Roger's duty to know of the company's default, and, therefore, he was liable to Burr for the dividends guaranteed on her stock.

(B) Duties of the surety or the guarantor toward the obligee.

20. The obligations of a surety or a guarantor depend upon those of the principal obligor. The surety or the guar-

antor is not bound to any greater extent than the principal. In order to learn the extent of the surety's or guarantor's liability, therefore, reference must be had to the contract between the principal obligor and the obligee. But it does not follow that the surety or guarantor is bound to the same extent as the principal, for his liability may be quite narrow under the terms of the contract.

1. Continuance of the Obligation

21. Usually a surety will continue liable for years unless he has fixed a time limit in his contract or unless a time may be implied when his liability will cease. If no such period is expressed or implied, a surety can seldom get a release from liability without the obligee's consent.

22. Where it is clear from the terms of the contract or from the transactions of the parties that the guaranty is to cover a running account, it is a continuing guaranty. Where the contract does not mention the period for which it is to hold good, it is usually presumed to be made for the particular transaction in view, and after obligations to the amount then contemplated have been contracted, the surety or guarantor is not to be held further liable unless the contract points plainly to a continuance of liability.

2. Joint Sureties or Guarantors

23. In the absence of an express agreement to the contrary, every surety is usually liable for the whole debt, no matter how many sureties there may be who are jointly bound. If one of several sureties pays the whole debt he may make the others contribute toward reimbursing him.

(C) Duties of the principal obligor toward a surety or a guarantor.

24. When, at the principal obligor's request, one becomes liable as a surety or a guarantor, ordinarily the principal is bound to compensate the surety or guarantor for any resulting loss. As soon as the surety or guarantor pays the obligee the amount due, he becomes entitled to receive from the principal what he has so paid. Upon payment by a surety or

guarantor of the whole amount due the obligee, the surety or guarantor becomes entitled by operation of law to the obligee's rights against the debtor. This privilege, called the right of subrogation, is denied to volunteers and strangers who officiously intermeddle when they have no interests to protect and are under no obligation to pay.

THE TERMINATION OF THE CONTRACT

25. Much of what was said in Part 4, Arts. **11-62,** under the heading of Discharge of Contracts applies to contracts of suretyship and guaranty here being treated. The five ways of discharging contracts there discussed, namely, by agreement, performance, breach, impossibility, and bankruptcy, will be used here as a basis for treating the discharge of the contracts we are now considering. Statements made hereafter about a surety must be understood to apply also to a guarantor unless the context indicates otherwise.

(A) Discharge by agreement.

26. The surety and the creditor may make an express agreement that the surety is no longer to be liable on his contract. Such an agreement must be under seal or supported by a consideration. See Part 1, Art. **61.** An agreement to discharge the surety is sometimes implied from the action of the creditor. Thus a voluntary discharge of the principal debtor discharges the surety also. But see Art. **32,** and Part 4, Art. **48.**

(B) Discharge by performance.

27. A surety will be released (1) by the principal obligor's performance of the undertaking, as by paying the debt where the contract relates to the payment of money, or (2) by the surety's performance of his contract of suretyship.

(C) Discharge by breach.

28. Any material change in the contract between the principal obligor and the obligee, made without the surety's knowledge and assent, will discharge him from liability.

29. An extension of the time of performance granted by the creditor to the principal debtor will discharge the surety. But this extension must be under seal or based upon consideration, and must be made without the surety's consent. Granting an extension of time to the surety, however, or even releasing him altogether, does not affect the principal's liability. The rule with respect to the discharge of a surety by granting him an extension of time is usually also applicable to a guarantor. The extension, in order to have such effect, must be without the surety's or guarantor's consent, and must be for a definite time and made binding on the creditor by a seal or a consideration. But if a guaranty is conditional, mere delay on the creditor's part may release the guarantor. See Art. **16.**

(D) Discharge by impossibility.

30. This is a matter of infrequent occurrence, and, therefore, of slight importance. The most obvious example is a guaranty of the performance of personal services. If the party from whom performance is looked for were to die, his surety would be discharged, unless otherwise expressly provided.

31. Usually a surety's death does not terminate his liability. His estate is ordinarily bound. But the death of one of several joint sureties may release his estate, though the others remain bound.

(E) Discharge by bankruptcy.

32. A surety may be released from his obligation by his own discharge in bankruptcy. But the discharge in bankruptcy of one of several co-sureties does not discharge the others. Neither does the principal obligor's discharge in bankruptcy release the surety.

INSURANCE

FIRE INSURANCE

33. Insurance on property is a conditional contract whereby one party undertakes to compensate another for loss or damage to property arising from some contingent event. The principle of indemnity is at the basis of all contracts of property insurance.

(A) Who has an insurable interest?

34. The nature of the contract of insurance on property makes it necessary that the insured have some interest in the property, either as owner or in some other capacity. One has an insurable interest when one is so situated with regard to the property that one will suffer a loss in case of its destruction by the peril insured against. But most fire policies require the insured to have more than a bare insurable interest. And the statements in Arts. **35-39** are subject to the qualification that the terms of any insurance policy may require the insured to be the sole and absolute owner of the property covered by it. See Tyree v. Insurance Co., in Art. **38.**

35. In general, it may be said that anyone who has a legal or equitable title to property has an insurable interest therein. Thus, bailees, common carriers, innkeepers, and warehousemen, have an insurable interest in property entrusted to their care. But there must be a real interest to protect. For example, a son who expects to inherit his father's property on the latter's death cannot during the father's lifetime insure the property for his own benefit. If the son takes out such insurance, however, and if no term of the policy requires an immediate insurable interest, he will be protected in case he becomes the owner of the property before the occurrence of a loss covered by the policy. See Art. **39.**

36. If a man enters into a contract of sale whereby he agrees to convey certain lands to another, each party has an insurable interest to protect. Mortgagor and mortgagee, landlord and tenant, all have insurable interests. A partner has an insurable interest in the entire firm stock. If a loss occurs, he must account to the firm on receiving payment from the insurance company.

37. Where a man has a right to occupy during his life certain property which, upon his death, goes to somebody else, he has an insurable interest in this property.

38. In states whose laws give a wife the exclusive use of her property free from the control and debts of her husband, the latter has no insurable interest in his wife's property. But when he is in possession of his wife's real estate with an inchoate curtesy right, he has been held to have an insurable interest therein. See Part 10, Art. **49.**

Tyree *v.* Insurance Co., 55 W. Va. 63 (1904). The Virginia Fire Insurance Company issued a policy to William F. Tyree insuring a house and some furniture. The policy provided that the company should not be liable if the title or interest of the insured were less than the entire, absolute, unconditional, unencumbered fee simple ownership. In fact the property was the separate estate of Tyree's wife. The West Virginia statute gives a wife sole control over her separate estate. Under it the husband has no right of possession during marriage and no curtesy initiate. A fire occurred and Tyree sued the Company. *Held* that he could not recover, for he had no insurable interest in the same.

Trade Insurance Co. *v.* Barracliff, 45 N. J. L. 543 (1883). The Trade Insurance Company issued to Barracliff a policy insuring real and personal property. Although the property belonged to his wife, the policy was taken out in Barracliff's name. When a loss occurred the insurance company defended a suit brought by Barracliff, alleging that he had no insurable interest. *Held,* he could recover. Barracliff had an insurable interest in his wife's property, because he was in actual possession and enjoyment thereof, and also because he had a reasonable expectation of the continuance of these pecuniary advantages as lawful incidents of his wife's ownership and his marital relations with her. In her realty he had, moreover, under New Jersey law, an inchoate curtesy right.

39. In the case of property insurance an interest must exist in the insured at the time of the loss. But it is not

necessary that the insured shall have had an interest at the time of the taking out of the policy, unless (as usually happens) its terms require such interest.

(B) Formation of the contract.

40. It is not necessary that a contract of insurance be in writing unless this is required by statute or the corporate charter of the insurance company which issues the policy. Whether oral or written the contract must contain all the essential elements of a contract. Oral contracts of insurance are often made in contemplation of a written policy, but in such cases all the essential terms must be clearly understood.

People's Insurance Co. *v.* Paddon, 9 Ill. App. 477 (1881). Paddon called at the office of the insurance company's agent, Miller, and left his policy book with a clerk without giving any directions about his insurance. The book was open at a page on which was written: "$2,500 on Empire not bonded 1,000." Afterwards he met Miller on the street and told him that he had left his policy book at the company's office with instructions about the insurance. A fire occurred and Paddon sued the company. *Held* that he could not recover. To make a valid oral contract of insurance the following things must be agreed upon: (1) the subject matter, (2) the risk insured against, (3) the amount, (4) the duration of the risk, (5) the premium. These matters not being understood, no contract existed.

41. The contract of insurance is one in which the utmost good faith is required of the insured. He must answer truthfully all questions put to him concerning the risk. He must also disclose all material facts the concealment of which would be a breach of good faith. The effect of concealing any material fact is to render the contract voidable at the option of the injured party. See Part 2, Art. **37.**

Burritt *v.* Insurance Co., 5 Hill (N. Y.) 188 (1843). Burritt was requested to mention all buildings within ten rods of the building on which he was applying for insurance. He failed to mention a cabinetmaker's shop which materially increased the risk. Although the omission was not fraudulent, the company refused to pay the amount of a loss which occurred later. Burritt sued. *Held*, Burritt's failure to mention the shop was fatal. He had been called upon to speak the whole truth. Had he told of the cabinetmaker's shop, the company either would not have made the contract at all or would have insisted on different terms.

42. When an insured makes a statement, voluntarily or in answer to an inquiry by the other party, he is obliged to speak the truth. The law requires that there shall be no misrepresentation. Even though made innocently, a misrepresentation avoids the policy.

Armour *v.* Transatlantic Fire Insurance Co., 90 N. Y. 450 (1882). The insurance company issued a policy on Armour's warehouse, by the terms of which other insurance was permitted without notice. It was provided that losses should be apportioned on the whole sum insured and that any misrepresentation whatever should avoid the policy. Armour's agent, Dickinson, who applied for the policy, mistakenly stated that there was already $200,000 insurance upon the building, although there was only $30,000 insurance. *Held* that the misrepresentation even though innocently made was material, and Armour could not recover. The insurance company's liability was greatly increased by the fact that there was only a small amount of additional insurance.

43. If an insured in good faith states his belief or expectation as to a future fact the policy will not be avoided although the event turns out contrary to the insured's belief or expectation.

Kimball *v.* Ætna Insurance Co., 9 Allen (Mass.) 540 (1865). When applying for fire insurance on his house Kimball stated that the house would be occupied soon and that he had a man in view who was going to occupy it. This statement was made in good faith, but the house was burned by an incendiary without having been occupied by any one. *Held* that Kimball could recover. His promise was made in good faith, and his failure to fulfil it would not avoid the policy in the absence of fraud.

44. A warranty is a representation which is made an essential part of the insurance contract. The effect of a breach of warranty is to make the policy void at the option of the injured party, no matter if the representation concerns an immaterial fact. A warranty as to location is binding, and in order for the insured to recover it must continue to be true during the term of the policy.

Lyons *v.* Providence Washington Insurance Co., 14 R. I. 109 (1883). The insurance company issued to Mary Lyons a policy of insurance against fire, on certain articles of furniture, and wearing apparel, "contained in house No.— McMillen Street, Providence, R. I." Lyons, without the knowledge or consent of the insurance company,

removed the articles to a house on Power Street, where they were destroyed by fire. The company refused to pay the loss and Lyons sued. *Held* that she could not recover. All material statements in insurance policies, including the location of the insured property, are warranties. They must be true and continue to be true during the life of the policy, or the insured cannot recover thereunder.

EXCEPTION.—Goods may be removed temporarily, as for example, a book from a library, or a wagon from a barn, without invalidating the insurance. The insured may recover if such articles are destroyed when they have been returned after removal, but usually not if they are destroyed while away.

(C) Conduct of the insured after the policy is issued.

45. An important provision in most policies is that any change in the interest, title, or possession of the property (otherwise than by the death of the insured), without the company's consent, shall avoid the policy. This clause against alienation is construed as far as reasonable in favor of the insured. Generally, immaterial changes of interest which do not increase the risk are outside the scope of this provision.

LOY *v.* HOME INS. CO., 24 Minn. 315 (1877). The insurance company insured Loy's dwelling house and its contents. The policy provided that it should be void in case of "a sale, transfer, or change in title." Loy mortgaged the premises and they were sold under foreclosure proceedings. After the sale, but before the period for redemption had expired, the loss occurred, Loy being still in possession. *Held* that Loy could recover. Neither the giving of the mortgage nor the sale of the premises on foreclosure, the time for redemption not having expired, effected any change in title or possession of the property under the proper interpretation of this clause.

46. Most policies provide that they shall be void if the risk is increased by any means within the control or knowledge of the insured, unless notice thereof is given the insurer. The risk may be increased either by a change in the structure or use of the property, or by the introduction of some practice which adds to the chance of loss.

WESTERN ASSURANCE CO. *v.* MCPIKE, 62 Miss. 740 (1885). The company insured McPike's dwelling against fire. McPike moved out and without his knowledge or consent the premises were used as a retail liquor store. The company refused to pay a loss, contending that the use of the building as a saloon constituted an increase of the risk.

Held that McPike could not recover. The manner in which the premises were used caused an increase of the risk.

Planters' Insurance Company *v.* Sorrells, 1 Baxter (Tenn.) 352 (1872). The insurance company insured R. P. Sorrells against loss by fire on a dwelling house. It refused to pay a loss on the ground of an increase of the risk by the use of the dwelling by W. H. Sorrells, a brother of the insured, as a boarding house. *Held* that the company was liable. The use of the premises as a boarding house did not constitute an increase of the risk.

47. Another provision is that against additional insurance. This applies to other insurance upon the same interest, so that parties whose interests are not identical, for instance, mortgagor and mortgagee, may insure without violating such provision. If there is no provision against other insurance, and other insurance is taken out on the same risk, the respective insurance companies are liable proportionately, all the policies being considered as one policy. Generally, taking out other insurance on the same interest, without the company's consent and in violation of a prohibitive clause, makes the policy void.

Funke *v.* Minnesota Farmer's Mutual Fire Insurance Co., 29 Minn. 347 (1882). The Minnesota Insurance Company insured the dwelling house and furniture of Funke against loss by fire for a period of seven years. The policy provided that it would be void if the insured should procure any insurance from any other company on the property insured without first obtaining the consent of the secretary of the Minnesota Company. Funke thereafter obtained insurance on the same property from another company. This last insurance, however, by reason of Funke's misrepresentations, was void. After a loss occurred Funke sued the Minnesota Company. *Held,* he could not recover. By making a subsequent agreement for the purpose of securing further fire insurance, without the Minnesota Company's consent, he avoided the policy even though he could not enforce the second insurance agreement.

48. The ordinary fire policy provides that it shall be void if a building therein described shall remain unoccupied or vacant for ten days. When the insured expects to close his dwelling for a time, as, for instance, when he is going to leave it unoccupied during the summer, he should get the company to consent to this by pasting a "rider" upon the policy agreeing to a temporary unoccupancy.

CONTINENTAL INSURANCE CO. OF NEW YORK *v.* KYLE, 124 Ind. 132 (1890). The insurance company issued a policy to Kyle insuring his dwelling house and its contents against loss by fire. The policy provided that it would be void if the house should become "vacant or unoccupied." Kyle's tenant moved out and Kyle rented the house to others. Before the new tenants moved in, but after they had made some slight repairs, the building burned down. The insurance company defended on the ground that the house was vacant and unoccupied. *Held* that there could be no recovery. Even though a certain supervision was exercised over the house, and though it might be said that possession in a certain sense had been taken by the new tenants, the house was vacant within the meaning of the policy, and the insurance was void.

49. The power to make conditions cannot be any greater than the power to disregard them. Therefore, the insurance company may waive a breach of any of the conditions of the policy. A waiver may be made by a duly authorized agent. Generally, however, the policy provides that "agents are not authorized to make, alter, or discharge contracts," so that the insured can be safe only in relying on the waiver of a general agent, and sometimes not even then.

WALSH *v.* HARTFORD FIRE INSURANCE CO., 73 N. Y. 5 (1878). A policy of insurance issued by the insurance company to Walsh provided that a waiver of any condition of the policy should be valid only when indorsed on the policy by an agent duly authorized to make such waiver. Walsh asked Crawford, the company's general agent, to waive a provision that the policy should be void in case the premises were vacant or unoccupied for more than fifteen days. Crawford agreed to do this, but neglected to indorse his consent to the vacancy on the policy, although he made a memorandum thereof in his insurance register. A fire occurred and Walsh sued the insurance company. *Held* that he could not recover. The mode of waiving the conditions of the policy was specified and Crawford's waiver was effective only when indorsed on the policy. Walsh was presumed to know of the limitation of Crawford's authority, and the latter's verbal waiver did not bind the company.

(D) What risks are insured against?

50. Most insurance policies provide that the insurance company "does insure . . . against all *direct* loss or damage by fire, except as herein provided." Under this clause it is held that a fire must be the proximate cause of the loss or damage. Where a building was damaged principally by the force of an explosion of gunpowder, it was held to be

proximately due to a fire which caused the ignition of the gunpowder and the burning of the powder itself, so that the insured was entitled to recover under the terms of his policy. So also where an insured building was damaged by the fall of an adjacent building which was on fire, although no part of the insured building was burned, the damage suffered was held to be proximately due to fire.

51. If a person removes goods from a burning building and puts them in an adjoining building, and the goods are lost or stolen by reason of the removal, the owner is entitled to recover under a fire policy if he had reasonable ground for thinking that the removal was necessary to save the goods from destruction.

52. A fire policy also protects the insured against fire losses arising from mere ordinary negligence or carelessness. But if a fire results from the insured's gross or reckless negligence or from his fraudulent or wilful misconduct or violation of law, the insured is not entitled to recover under the terms of his policy. For example, where a fire resulted from a ship captain's use of turpentine as fuel, in wilful violation of the law, while racing his boat, no recovery could be had against a fire insurance company.

(E) The transfer of the policy.

53. A fire insurance policy may be transferred with the consent of the company. Ordinarily, where insured property is conveyed and nothing is said about the insurance, the purchaser does not acquire title to the insurance policy, and the insurance comes to an end. If after the transfer the property is destroyed by fire, the seller cannot recover on his policy of insurance because he no longer has any interest in the property. The purchaser cannot recover because he never made a contract of insurance with the company. In purchasing real estate, therefore, it is often wise for the purchaser to contract for a transfer of the insurance policy at the time of the delivery of the deed.

54. A fire insurance policy may not be transferred without the insurance company's consent before a loss occurs, because in making a contract of insurance the company is supposed to regard the personal character of the insured. While the company may be willing to insure A, it may not be willing to insure B. See Part 3, Art. **8.** The sale of the insured property without the company's consent generally avoids the policy. But if the company assents to the seller's assignment of the policy to the purchaser, this constitutes a new and original contract between the company and the purchaser.

55. While the insurance policy may not be transferred without the company's consent before a loss has occurred, after the property has been destroyed or damaged by fire, the liability of the company is fixed, and the owner of the policy may transfer it without the consent of the company.

(F) Notice and proof of loss.

56. Most fire policies provide that the insured shall give the company "immediate notice" in writing of the occurrence of a fire, and furnish the company within sixty days "satisfactory" proof of loss.

57. The requirement as to immediate notice of the happening of a fire is construed to mean that the insured must be reasonably diligent in notifying the company thereof as soon as possible under the circumstances. The same construction is given to requirements that notice shall be given "forthwith" or "as soon as possible."

58. The general rule is that a failure to furnish proofs of loss within the required period does not operate as a forfeiture of the insured's rights under the policy, unless it is expressly provided that such failure shall render the policy void or that no action shall be maintained on the policy unless all its conditions have been complied with.

59. The company may waive notice and proof of loss. If it does this either expressly or impliedly, and gives the insured good reason to believe that it does not intend to insist upon such notice and proof, he is not bound to give them.

60. Where the insured in good faith furnishes proof of loss, which he believes to be sufficient, but which in fact contains some defects, it is the company's duty to make objection promptly if it intends to rely on such defects. Failure to object will justify the insured in supposing that he has filled the requirement.

Bumstead *v.* Dividend Mutual Insurance Co., 12 N. Y. 81 (1854). Bumstead was insured in the Dividend Mutual Insurance Company. The policy provided that in case of loss the insured should deliver to the company a sworn statement thereof, verified, if required, by books of account and other proper vouchers. The insured's property, account books, and vouchers were all destroyed, and Bumstead made an honest general statement of his loss with the best additional evidence he could give. Later on the insurance company refused to pay the loss. Bumstead brought suit. The company defended on the ground that he had not furnished proofs of loss in the manner required by the policy. *Held,* he could recover. The acceptance of the proofs furnished by Bumstead without objection involved a waiver of any technical defects.

LIFE INSURANCE

61. Life insurance is a contract whereby one party, called the insurer, promises to pay a certain named sum to a second party upon the happening of a certain death or at a designated time, in consideration of definite payments, called premiums, made regularly to the insurer. The sum may be payable to the one whose life is insured, to his executor or administrator, to a person designated by him, or to certain others having an insurable interest. The person to whom the insurance money is payable is called the beneficiary.

(A) Who has an insurable interest?

62. The requirement of insurable interest is based upon that principle of public policy which prohibits wagers. Obviously it would be unwise to permit a man to insure another's life when thereby he would be more interested in having that life brought to an end than in having it continued. Therefore, the law generally ordains that when one insures another's life he must be so situated, either by relationship or business dealings, toward the person whose life is insured that he will

have an interest to preserve the life in spite of the insurance. But in New Jersey it appears that an insurable interest is not required in life insurance. Contrary to the rule in property insurance, the interest must in life insurance exist when the policy is taken out. The fact that the interest afterwards ceases to exist does not invalidate the life insurance.

63. Where a man insures his own life and pays the premiums, he may name as beneficiary one who has no insurable interest in his life. Where the premiums are paid by the beneficiary, however, he must have an insurable interest. A man has an insurable interest in his own life to any amount he chooses to pay premiums on. Certain relationships by blood or marriage, and certain commercial transactions give people insurable interests in the lives of others.

64. Ordinarily, no matter how closely two people are related, neither has an insurable interest in the other's life by mere virtue of relationship alone. There must be an expectation of pecuniary benefit. For example, a parent has an insurable interest in the life of his child on the ground that he is entitled to the child's earnings during minority, and that on reaching full age the child is liable to be called on to contribute to his, the parent's, support. A sister has an insurable interest in the life of a brother who supports her.

65. Husband and wife have an insurable interest in each other's life. Each has a pecuniary interest in the other; the wife is entitled to support, and the husband is entitled to his wife's services. A woman has an insurable interest in the life of her betrothed.

Chisholm *v.* National Capitol Life Insurance Co., 52 Mo. 213 (1873). Harriet Chisholm was engaged to marry Robert Clark. She took out a policy of insurance on his life payable to her as his intended wife. When Clark died the company refused to pay on the ground that Chisholm had no insurable interest in Clark's life. She sued on the policy. *Held* that Chisholm could recover. She had an insurable interest in Clark's life, a valid contract to marry existing between them. Had he lived and violated the contract, she could have sued him for damages for breach of promise. Had the engagement to marry been performed, then as his wife she would have been entitled to support.

66. When a person acquires a commercial interest in the life of another, he may protect that interest by insurance. A creditor may insure his debtor's life, a partner his co-partner's, and a surety the life of his principal. But a creditor in insuring the life of his debtor must take care that the transaction does not become a mere wagering contract. In order to prevent speculation on the debtor's life a creditor will not be allowed to recover on a policy on a debtor's life in an amount wholly disproportionate to the amount of the debt. He may take out a policy for an amount which will give him reasonable protection under the circumstances, but the amount of the policy must not be so greatly in excess of the debt that it is clear he is wagering upon his debtor's life.

CAMMACK *v.* LEWIS, 15 Wall. (U. S.) 643 (1873). John E. Lewis owed $70 to Cammack, which he was not able to pay. At Cammack's suggestion Lewis insured his life in the New Jersey Mutual Life Insurance Company for $3,000, Cammack paying the first premium and agreeing to pay the others. Lewis then assigned the policy to Cammack. Lewis died seven months afterwards and Cammack collected $3,000 from the company. Lewis's administratrix, Maggie Lewis, then sued Cammack to recover this insurance money. *Held* that she was entitled to receive from Lewis the $3,000, less the amount of his debt and the premium paid. As far as Cammack was concerned, insurance of $3,000 to secure a debt of $70 was a mere wager. The disproportion between Cammack's real interest and the amount to be received by him deprived it of all semblance of being an honest effort to secure the payment of his debt.

(B) Formation of the contract.

67. Much of what has been stated about the formation of a contract and the interpretation of the policy in property insurance is generally applicable to life insurance. In some states it is at least doubtful whether or not private individuals have the right to issue policies of life insurance, and the insurance departments of the various states seldom license individuals to do so.

68. The concealment of any material fact usually avoids a policy of life insurance. A fact is material if knowledge of it would influence the parties in making the contract. It is not necessary that it should increase the risk or contribute to

the loss. The insurer ought to scrutinize very carefully the answers in the application. If the applicant neglects to answer a question or answers it imperfectly the issue of a policy by the insurer may be deemed a waiver of such neglect or imperfection. See Art. **41.**

Phœnix Insurance Co. *v.* Raddin, 120 U. S. 183 (1886). Sewell Raddin applied for insurance on the life of his son, Charles E. Raddin. In answer to four interrogatories as follows: "Has any other application been made for assurance? If so, with what results? What amounts are now assured on the life of the party? And in what companies?" Raddin replied, "$10,000 Equitable Life Assurance Co." In an action on the policy the company defended on the ground of the intentional concealment by Sewell Raddin of the fact that within three weeks before the issue of the policy he had applied to two other companies for additional insurance on his son's life each of which had declined to take the risk. *Held* that the answers were not warranties but representations which were required to be substantially true. However, as this question appeared to be imperfectly answered the issue of the policy without further inquiry was a waiver of the imperfections of the answer and rendered the omission to answer more fully immaterial. Therefore, Raddin was allowed to recover.

69. All statements in life insurance policies are regarded as being made at the time of the delivery of the policy to the insured. If, therefore, between the time of signing his application and the delivery of the policy any change takes place in the insured's condition he should disclose this fact to the insurance company. A change in the insured's condition, whether made known to the company or not, may have the effect of invalidating the insurance.

Cable *v.* U. S. Life Insurance Co., 111 Fed. 19 (1901). Cable applied to the insurance company for a life insurance policy. In his application he warranted that he had never had pneumonia and further agreed that the policy should take effect only upon "payment of the first premium and delivery of the policy during his lifetime, sound health and insurable condition." When the policy was ready and tendered to Cable he refused to accept it on the ground that he wanted to consult with his friend George S. Lord. Shortly afterwards Cable was taken ill with acute pneumonia. Three days later the company's solicitor tendered the policy to Lord as Cable's agent, who accepted the same and paid the first premium. The solicitor asked Lord how Cable was and Lord said, "No worse than he has been for the past forty-eight hours." The company had no knowledge of Cable's illness until after his death

five days later. The company refused to pay the amount of the policy and Cable's administratrix sued. *Held* that she could not recover. It was the duty of Lord as Cable's agent fully to disclose his condition. His partial statement was misleading and not such as to put the agent on inquiry. The delivery of the policy under such circumstances did not create a contract of insurance even though Lord was not guilty of intentional fraud.

70. Failure to pay the first premium in the case of life insurance generally prevents the policy from taking effect, while failure to pay subsequent premiums gives the company the right to declare a forfeiture of the policy. Hence, a person paying the premiums on a life insurance policy should be careful to pay before the last day for payment expires.

(C) Beneficiaries.

71. Where a person insures his life and designates another as beneficiary, usually he has no right to change the beneficiary so as to make the policy payable to somebody else without the original beneficiary's consent, unless he has expressly reserved that right. But if the person whose life is insured avoids the policy in any way, the beneficiary may not recover from the company.

72. The beneficiary has a vested interest in the policy, except in Wisconsin, and even though he should die before the person whose life is insured, the proceeds of the policy will pass to the beneficiary's estate rather than to the estate of the one whose life is insured. But ordinarily the latter, when taking out the insurance, may reserve the right to change the beneficiary. If he fails to change the beneficiary, however, and thereafter dies, the beneficiary or his estate is entitled to the insurance money.

Central Bank of Washington *v.* Hume, 128 U. S. 195 (1888). Thomas L. Hume, while insolvent, insured his life, naming his wife and his children as beneficiaries. When Hume died, he was heavily indebted to the Central Bank. His widow collected the insurance money and the bank sued her to have it applied to the payment of Hume's debt. *Held*, the wife and children took a vested interest in the proceeds of the policy, of which Thomas L. Hume could not deprive them. Neither have the personal representatives or the creditors of the

insured any interest in the proceeds of such policies, which belong exclusively to the beneficiaries to whom they are payable.

73. But in any case the beneficiary's rights depend largely upon the terms of the policy. He may get a vested interest in the policy as above set forth, or the policy may provide that his interest therein shall be defeated by the happening of some event, as, for instance, his death during the lifetime of the insured.

(D) Suicide; execution for crime.

74. Most policies provide that they do not cover death by the hands of the insured or by the hands of justice, or in the course of a violation of the law. In the absence of such provision, usually the policy will not be avoided in case the insured commits suicide, if the policy is payable to a designated beneficiary, and not to the estate of the insured. The reason of this rule is that suicide is regarded as one of the risks assumed by the insurer. But in the United States courts and the New York courts the rule does not obtain, and suicide avoids the policy.

Patterson *v.* Natural Premium Mutual Life Insurance Co., 100 Wis. 118 (1898). Patterson insured his life, naming his children as beneficiaries. Four months later he committed suicide. The company defended on the ground that suicide, while Patterson remained sane, was not a risk covered by the policy. *Held* the beneficiaries could recover. Since third persons were the beneficiaries, Patterson's intentional self-destruction while sane did not avoid the policy in the absence of any provision therein to that effect.

75. Even though a policy fails to provide that the insurer shall not be liable in case of the death of the party whose life is insured at the hands of the Government, the beneficiary cannot ordinarily enforce payment if the death occurs by reason of execution for crime.

(E) Notice and proof of death.

76. Life insurance policies generally require immediate notice to the company of the death, and the furnishing of satisfactory proof thereof. See Arts. **57-60.**

AMERICAN BUSINESS LAW
(PART 10)

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THE MANAGEMENT OF DECEDENTS' ESTATES

THE GRANTING OF AUTHORITY TO ADMINISTRATORS AND EXECUTORS, AND THE REVOCATION THEREOF

1. In this Section we shall consider the duties of those who take charge of the estates of decedents from the time they qualify until they file their final accounts. An executor is a person appointed by the testator to take charge of his estate. An administrator is a person appointed by public authority to take charge of the estate of a decedent who did not appoint an executor, or whose executor has not wound up the estate.

2. An executor is appointed by will. But he does not derive his authority entirely therefrom. To establish his authority, it is usually required that the one appointed shall signify his acceptance of the appointment by proving the will, taking oath to perform his duties as executor, and receiving letters testamentary from the public official who has charge of such matters. The letters testamentary constitute a certificate of the executor's authority.

(A) Proving the will.

3. The duty of proving the will rests upon the person who is thereby appointed to take charge of the decedent's estate. Therefore, an executor should duly offer the will for probate

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in the probate court. If an executor has the will in his custody, but does not desire to qualify as executor, he should formally renounce the office of executor, and file the will safely in the proper public office. When the executor renounces or does not qualify, the probate court may appoint an administrator with the will annexed. If the executor fails to prove the will, any person having a valid interest therein may offer it for probate.

4. To get a will admitted to probate it must be formally proved in the probate court. This task is begun by filing a petition for probate. If the executor makes the petition, usually he states therein that he is the executor named in the will, and sets forth the place and the date of the decedent's death, together with his last domicile, the estimated value of the property, and the respective names and residences of the surviving spouse and next of kin. He also states that the instrument offered is the decedent's last will and testament, and asks to be confirmed as executor. Usually the will may be admitted to probate without further procedure other than proof by the oaths of one or more of the witnesses of the fact that the testator signed the will. In many states, however, when an executor offers the will for probate, notice must be given to interested parties either personally or by advertisement. If it appears that the parties interested do not object, ordinarily probate will be granted upon the testimony of one or more witnesses.

(B) Qualifications of executors and administrators.

5. The next question to be treated concerns the appointment of executors and administrators. In the case of a will, the naming of the executor is done by the decedent who has made the will. If a decedent has died without a will, the widow or the widower is first entitled to receive a certificate of authority to manage and settle the decedent's estate. This certificate is called the letters of administration. If there is no surviving spouse, the persons entitled are the nearest relatives who under the statute of distribution of the particular state would

receive the residue of the personal property, or a share thereof, after payment of debts. In general, it may be said that the order of preference is as follows: first, widow or widower of the decedent; second, children; third, grandchildren and other lineal descendants; fourth, father or mother; fifth, brothers and sisters; sixth, descendants of deceased brothers and sisters; seventh, grandfather or grandmother; eighth, uncles or aunts; ninth, cousins; tenth, creditors or other proper persons.

6. Valid reasons may justify a departure from this order in certain cases. For example, one who occupies a hostile position toward the estate should not be appointed. Neither should minors, drunkards, weak-minded or insolvent persons be appointed. When persons are in the same degree of relationship to the decedent, males are generally preferred to females. The older one of two applicants is often chosen when there is no better way to decide between them.

(C) Various kinds of executors and administrators.

7. If the decedent's will does not name an executor, or the person named is unable or unwilling to act, an administrator *cum testamento annexo* (with the will annexed) is appointed. Such an administrator is generally called an administrator c. t. a. The administrator c. t. a. differs from an ordinary administrator in that his duties are sometimes marked out by the terms of the will, while an ordinary administrator has no will to guide him.

8. If an estate has been partially wound up by an administrator, who dies or is removed before he has fulfilled all his duties, it becomes necessary to appoint a successor. This successor is called an administrator *de bonis non,* whose duty it is to manage and wind up the affairs of the estate not already settled by the first administrator. If a decedent has left a will, and his executor or administrator has died or been removed before the estate is wound up, the successor is called an administrator *de bonis non cum testamento annexo.* The duty of this

administrator is to finish the work left uncompleted by his predecessor, pursuant to the terms of the will.

9. An administrator *pendente lite* is an administrator who is appointed to take charge of the affairs of an estate pending the settlement of a dispute concerning the estate which has arisen among the interested parties. An administrator of this kind proceeds with the settlement of the estate, and as soon as it is learned which of the disputants is in the right, a regular executor or administrator is appointed and the administrator *pendente lite* turns over the estate in his hands to his successor.

10. In several of the states an officer designated as the "public administrator" is appointed by law to administer the estates of decedents in certain cases. He may be entitled to act in estates where the decedent has left no relatives, or where the relatives refuse to act, and in certain other proper cases. In general his duties are similar to those of an ordinary administrator.

11. An executor *de son tort* is a person who wrongfully intermeddles with a decedent's estate and presumptuously takes it upon himself to manage its affairs. Since he has assumed to be an executor, he is liable to the rightful executor or administrator for whatever property belonging to the estate comes into his hands. While he is not entitled to compensation for his services, he may claim credit for sums disbursed by him to the extent that the recipients of such sums were entitled to share in the distribution of the decedent's estate.

(D) Bonds of executors and administrators.

12. In almost all cases administrators are required to file bonds for the faithful performance of the duties of their office. In most of the states executors are also required to file bonds for the faithful fulfilment of their duties unless the filing of such bonds is expressly dispensed with under the terms of the will.

(E) Revocation of the authority of executors and administrators.

13. The ordinary rules applicable to any fiduciary apply in the case of executors and administrators. For any breach of the duties of their trust they may be removed by the power which appointed them. An application for their removal may be made by any person having an interest in the estate. The authority of an executor or an administrator is subject to revocation for any act of gross neglect or wilful misconduct, such as the use of his position to obtain an unlawful personal profit.

THE DUTIES OF EXECUTORS AND ADMINISTRATORS AFTER THEY HAVE QUALIFIED

14. Generally executors and administrators have much the same duties, except that administrators are not ordinarily required to prove a will. *Hereafter when mention is made of an executor it must be understood that the remarks apply to an administrator also.* In general the duties of an executor are as follows: (1) to bury the decedent; (2) to give public notice of his appointment; (3) to file an inventory and appraisal; (4) to collect what belongs to the estate; (5) to pay the decedent's debts and the costs of administering the estate; (6) to pay the succession taxes and other taxes in proper cases; (7) to file an account; (8) to have his account settled; (9) to distribute the balance in his hands among the persons entitled. We shall consider briefly each of these duties in the order followed above.

(A) The first step: to bury the decedent.

15. The first duty of the executor is to see that the decedent's body is disposed of in accordance with the wishes expressed by the decedent. If the decedent has not made known his wishes as to the mode of burial, the executor should see that his remains are buried in a manner suitable to his circumstances and station. It often happens, however, that the decedent is buried before the executor qualifies, and even before the contents of the will are known.

(B) The second step: to give public notice of one's appointment.

16. After the executor has been appointed, and has fully qualified, public notice of his appointment must be given, by advertisement or otherwise. The purpose of this is to expedite the settlement of the estate by promptly informing creditors and other interested parties as to such appointment.

(C) The third step: to file an inventory and appraisal.

17. The laws of every state require an executor to make and file, or cause to be made and filed, within a fixed time, an inventory and appraisal of the decedent's goods and credits. If this is done, and the executor learns subsequently of other assets belonging to the estate, an inventory and appraisal of them should be made and filed. But in some states he is required only to account for after-discovered assets, without being obliged to file an inventory and appraisal of them.

18. The inventory and appraisal should include all bonds, notes, and other evidences of debt due the decedent, as well as all other claims and demands for money, and all kinds of personal property owned by the decedent at the time of his death. If the executor himself owes the decedent any money he should include his own debt in the list.

(D) The fourth step: to collect what belongs to the estate.

19. The executor should gather in all the personal property belonging to the estate. This includes moneys due on life insurance policies which are made out in favor of the decedent or his estate. If an life insurance policy is payable to the decedent's widow or children, usually the executor has no right to the proceeds, for such policies belong to the beneficiaries. See Part 9, Art. **72.**

20. If the decedent has been in business for himself, the executor, as a rule, should close the business out as soon as possible. A delay in doing this, however, may be justified if the executor finds it necessary to run the business for a while

in order to avoid the heavy loss sometimes incident to a sudden liquidation. The executor of a deceased partner has nothing to do with partnership effects. The right to liquidate the firm's affairs belongs to the surviving partner. See Part 5, Arts. **88** and **89.**

21. An executor generally has nothing to do with real estate unless special authority is conferred by the will. In the absence of such authority he should not collect rents accruing after the decedent's death. But he should collect arrears of rent which have fallen due in the decedent's lifetime. If the decedent in his lifetime has made a contract to sell certain real estate, but the deed has not been executed, it is considered that the decedent has converted the real estate into personalty, and, if the contract is afterwards carried out, the executor will be entitled to the proceeds of the real estate.

22. Usually an executor should not undertake to invest the funds coming into his hands. His duty is to wind up the estate. When he converts property into cash he should promptly deposit the cash to the credit of the estate with some responsible banking institution. Sometimes, however, where the estate will remain unsettled for years, he may invest money in his hands, in order to make it more productive.

(E) The fifth step: to pay the costs of administering the estate and the decedent's debts.

23. It is the duty of the executor to pay the decedent's debts. Whenever possible, he should pay debts promptly in order that interest may not be charged, but if the estate is insolvent he must beware of paying any creditor more than his proper share. In many states certain debts are entitled to priority in payment. Generally, the order of preference is about as follows: (1) funeral expenses and costs of administration; (2) expenses of the decedent's last illness; (3) judgment debts in some states; (4) servants' wages not exceeding one year in Alabama, Arkansas, California, Delaware, Illinois, Indiana, Kansas, Maryland, Massachusetts, Missouri, Montana, North Carolina, Ohio, Oregon, and Pennsylvania; (5) in

Georgia, Maryland, New York, Pennsylvania, and South Carolina claims for rent not exceeding one year.

24. Where the personal property is insufficient to pay all the debts it is necessary to sell real estate to make up the deficit. Usually the real estate goes directly to the relatives in case there is no will, and to the persons to whom it is left in case there is a will. The testator may give his executor an express power to sell real estate to pay debts in case the personal estate is insufficient for that purpose.

25. In all the states statutes confer upon the court which has supervision of decedents' estates power to order the sale of a decedent's real estate for purposes of administration, such as the payment of debts. The statutes designate the person who may apply for such an order. Generally the right is conferred upon the executor or the administrator and creditors of the decedent. Usually the time within which an application must be made is fixed by law. If no time is so fixed, the application must be made within a reasonable time.

(F) The sixth step: to pay the succession taxes and other taxes in proper cases.

26. Often an executor must pay taxes for which the decedent was personally liable at the time of his death. Such taxes may be considered as debts due by the decedent. Executors are mostly concerned with the payment of succession or inheritance taxes. While these taxes are really payable by the beneficiaries, it is usually the executor's duty to see that they are paid.

27. Succession or inheritance taxes are those imposed by government upon the privilege of taking and enjoying the property of a decedent. They are payable with certain exceptions by all beneficiaries to whom any interest in the estate of a decedent is transmitted. See Art. **46.** The rate of taxation varies in different jurisdictions from one to five per cent. or even more. Usually these taxes are only imposed on estates where the net amount passing to beneficiaries exceeds a certain

minimum, which varies in the different states, for the most part ranging from $250 to $1,000.

28. In general, succession taxes are imposed on every interest passing to an heir or other beneficiary, although certain classes of persons are exempted by the express terms of some statutes from payment of these taxes. The parents, widow or widower, children and other descendants of the decedent born in lawful wedlock are exempted from the payment of some succession taxes. In certain states charitable, educational, and religious institutions are also exempted.

29. A legacy given and accepted in full satisfaction of a debt is not usually taxable, except in New York. But where there was no legal obligation upon the decedent to pay and the legacy is given as a gratuity for services rendered without expectation of reward, it will be subject to the tax.

30. The inheritance of real estate is usually subject to a tax imposed by the state where the real estate is located. The succession to a decedent's personal property is usually subject to a tax imposed by the state where the decedent has been domiciled.

31. Moreover, a United States tax, called the Federal Estate Tax, is payable on an estate whose net value, after providing for debts and expenses of administration, exceeds $50,000.

32. An executor should be prompt in giving the notices and making the payments required by the tax laws. Otherwise, he may incur heavy penalties.

THE ACCOUNTS OF EXECUTORS AND ADMINISTRATORS, AND THE FINAL STEPS IN CLOSING AN ESTATE

(A) The seventh step: to file an account.

33. An executor is bound to keep an accurate record of all moneys and properties belonging to the estate which come into his hands, and also of all payments and disbursements made on account of the estate. It is generally further incumbent upon him to file in a designated office within a certain time an account of his administration of the estate, showing all receipts and disbursements. If the executor fails without just cause to file his account within the required time, any party in interest, as, for example, a creditor, an heir, or a legatee, upon application to the probate court, may obtain an order directing the filing of an account. His failure to file an account after such order may subject him to revocation of his letters of authority, to fine or imprisonment for contempt of court, and to prosecution by indictment.

1. Debit Entries

34. In general an executor must account for all the assets of the estate which have come into his hands as executor. The inventory and appraisal is usually the basis of his account. Therefore, he is charged with the amount of the appraisal. However, he may show that the property inventoried turned out to be worth more or less than the amount set forth. All this appears in his account of principal.

35. Besides the personal chattels listed in the inventory and appraisal the executor should charge himself with all income received therefrom. These items of income should be stated apart from the account of principal.

36. In the absence of special authorization to deal with real estate, he does not come into possession thereof, and since he does not receive the rents he cannot be called upon to account for them.

37. An executor is a fiduciary. If, therefore, he uses the funds of the estate and earns interest thereon he will be charged in his accounting with the interest earned. If he embarks the funds of the estate in business for his own purposes, the beneficiaries may in some jurisdictions elect to charge him either with legal interest or with the profits made by him. If an executor mingles the estate's moneys with his own he may be charged with interest thereon because it will be presumed that he must have used the moneys. And, if as a result of such intermingling, it is impossible to tell how much belongs to the estate and how much to the executor personally, the estate will be entitled to the whole.

2. Credits and Disbursements

38. In general, an executor is entitled to credit for all reasonably necessary expenses incurred by him in the administration and settlement of the estate. In order that credits claimed by the executor may be allowed it should appear that: (1) the expenses were incurred in good faith; (2) they were reasonable in amount; (3) they were not made necessary by the executor's misconduct. The expenses for which credit may be claimed by an executor vary in accordance with the size of the estate and the transactions necessary to settle it. The items for which credits are most commonly claimed will be briefly treated under the following subdivisions: (*a*) expenses of administration, (*b*) debts of the estate, (*c*) compensation of executors and administrators.

39. (*a*) *Expenses of Administration.*—Proper items of credit under this head include the cost of proving the will, if any, and of letters testamentary or letters of administration, fees paid to appraisers, and for advertising, and generally all legitimate expenses involved in managing, preserving, and settling the estate.

40. In many cases, executors are not entitled to allowances for sums paid to their agents and other employes. This is for the reason that executors are paid for their own services and ought not to expect double compensation when they delegate

their duties. However, extraordinary circumstances may justify the employment and remuneration of agents and other persons. The expediency of such employment is a matter to be determined by the court. The employment of a lawyer to advise the executor is proper, and the estate is liable for a reasonable attorney's fee.

41. (*b*) *Debts of Decedents.*—An executor should pay, and in his account claim credit for, all legal debts due by his decedent. Where any debt arises out of a contract made by the decedent in his lifetime which could be enforced against him if living, it is a legal debt against the decedent's estate and should be paid by the executor. In addition to this any debts properly contracted by the executor in the administration of the estate constitute debts of the decedent's estate which should be paid, and for which credit should be claimed by the executor. Credits may be claimed for the cost of the religious ceremonies in connection with the funeral, the price of a burial lot and a tombstone, provided these are in keeping with the decedent's circumstances. See Art. **23.**

42. (*c*) *Compensation of Executors.*—In all the states except Delaware an executor is entitled to a fair compensation for the value of his services in settling the estate. His claim for compensation is one of the expenses of the administration, and is generally payable even before debts and legacies. There is no fixed rule as to the amount of such compensation. It is determined by the allowance of the court which supervises the executor's accounts, or by a local statute on the subject, or by a recognized local custom fixing the commissions at a certain rate, as, for example, three or five per cent.

(B) The eighth step: to have one's account settled.

43. When an executor has prepared his account he should present it for filing, recording, and auditing in the probate court. The probate officer who has charge of the settlement of estates may be designated as Judge of the Probate Court, Judge of the Orphans' Court, Register or Registrar of Wills, or Surrogate, but, whatever his title, his duties are generally

much the same. After the account has been duly filed and recorded it is audited or approved by the probate officer. If any errors or irregularities appear in it, they should be pointed out and corrected.

(C) The ninth step: to distribute the balance in one's hands among the persons entitled thereto.

44. If no errors or irregularities appear, the account is approved in accordance with the statute of the state wherein it is filed, and the executor is ordered to distribute the balance remaining in his hands among the parties entitled. He then has a right to be discharged from the office of executor.

THE INTESTATE LAW, WILLS, AND TRUST ESTATES

THE INTESTATE LAW

45. Sometimes a will is called a testament, and the man making it is called a testator. If he leaves no will he is said to die intestate. The intestate laws of the state in which his realty is situated govern the distribution of his real estate. The intestate laws of the state in which he was domiciled govern the distribution of his personalty. What is here said with reference to the descent and distribution of property in cases of intestacy must be understood as being qualified by various state statutes concerning partnerships, homesteads, and widows' and children's exemptions, as well as being subject to creditors' rights.

46. The laws with regard to the devolution of property in case of intestacy differ in the various states. In general, it may be said that the order of succession, subject to the rights of the surviving husband or wife, is as follows: (1) to the intestate's children and other descendants; (2) in default of lineal descendants, to the parents of the intestate; (3) to the intestate's brothers and sisters; (4) to other remoter relatives of the intestate.

(A) The rights of the widow.

47. Formerly when a man died intestate, ordinarily his widow was entitled to one-third of his real property for life and one-third of his personalty absolutely if he left issue, and to one-third of his realty for life and one-half his personalty absolutely if he left no issue. The laws of the different states have varied these rules in certain particulars.

48. When the husband dies leaving issue, the widow is now usually entitled to all or part of her deceased husband's personal estate absolutely and to part of his real estate for life or absolutely. When the husband dies leaving no issue, the widow is ordinarily entitled to one-half the personal estate absolutely and one-half the real estate absolutely or for life. Where the husband leaves neither issue nor other relatives, the widow often gets the entire estate, both real and personal.

(B) The rights of the widower.

49. Formerly a surviving husband was entitled to all his deceased wife's personal property absolutely and all her real estate for the rest of his life. Now he usually gets an absolute or life interest in all or part of his wife's real estate and all or part of her personal estate absolutely. In Illinois, Iowa, Missouri, and Tennessee, he gets one-half her real estate absolutely. In Maine he is entitled to one-third of it absolutely. In Florida and Mississippi the husband gets all the property, real and personal, absolutely. In Massachusetts he gets real estate to the amount of $5,000 in value. If his wife leaves neither issue nor other relatives, the husband generally gets her whole estate, and in some states this is the case when she dies without issue or a parent surviving her.

(C) Children and other descendants.

50. Subject to the rights of the surviving spouse, if an intestate leaves children, the children share equally in the real and personal estate of the decedent and take it absolutely. The issue of a deceased child represent the parent and take the share to which he or she would have been entitled.

51. Subject again to the rights of the surviving spouse, if the intestate survives his children and leaves grandchildren but no other lineal descendants, then all the grandchildren share the estate among them equally. If any grandchild has died leaving issue, these great-grandchildren take the share of their deceased parent.

(D) The father and the mother.

52. Subject to the surviving spouse's rights, where there are no lineal descendants, the property of an intestate goes, in many states, to the father. In some states it goes to the father and the mother jointly or to the survivor of them. Usually where a child who has inherited real estate from one parent dies, leaving the other parent surviving, the surviving parent cannot inherit such real estate from the child, but many states have abandoned this rule.

(E) Brothers and sisters and their descendants.

53. Subject to the surviving spouse's rights, if an intestate leaves neither issue nor parent, the property generally goes to his brothers and sisters and their descendants.

(F) Other relatives.

54. In default of any of the above mentioned relatives, the property of an intestate usually goes as follows: (1) To the grandparents or such of them as may survive the intestate; (2) if there is no surviving grandparent, then to uncles and aunts or their descendants; and (3) if there is no surviving representative of this class of kindred, then to more distant collateral relatives. If a decedent dies without leaving a surviving spouse and there are no other kindred of any description, his property goes to the state. This is called *escheat.*

WILLS

55. The law relating to wills is extremely technical in some particulars, so that great care should be taken in drawing a will. A will is defined as a legal declaration by a man or a woman designating who shall possess and enjoy his or her property or certain parts of it after his or her death.

(A) Who may make a will.

56. In general, every person of full age and sound mind who is not under some legal disability may make a will. In practically all the states statutes now confer on married women the power to dispose of their property by will, subject to the husband's rights as tenant by the curtesy in his wife's estate. See Art. **49.** A husband, by his will, may exclude his wife from participation in his estate except to the extent that the law entitles her to share therein. See Art. **48.** Either husband or wife may cut off children or other relatives entirely by will.

(B) Various kinds of wills.

57. In general all wills must be in writing. A holographic or olographic will is one written entirely in the testator's own handwriting. In some states holographic wills, unlike ordinary written wills, need not be signed by subscribing witnesses, but may be proved by witnesses familiar with the testator's handwriting.

58. In all the states except Connecticut and Louisiana, one is allowed to dispose of at least a certain amount of personal property by an oral will. This is called a nuncupative will. A nuncupative will must be made during the testator's last illness in anticipation of imminent death, and must be reduced to writing within a fixed period, usually six days after the words constituting the same were spoken, and must be offered for probate with the same formality as is required in the case of a written will.

(C) Formal requisites.

59. *Writing.*—Except as stated in Art. **58** a will must generally be in writing. But it may be typewritten or printed.

60. *Signing.*—A will must be signed by the testator. If the testator is illiterate or physically unable to write, he may sign by making his mark. Ordinarily the signature should be at the end of the will. If the will is contained on several sheets of paper it is a wise precaution to have the testator sign

each sheet of paper in addition to signing at the end of the will.

61. *Publication.*—In a few states it is required that the testator shall declare to the attesting witnesses, when they sign the instrument, that he intends it to operate as his will, and shall request them to sign it as witnesses. It is wise to observe these formalities in all the states.

62. *Acknowledgment.*—Where a testator does not actually sign the will in the presence of the witnesses, but calls them in afterwards, it is usually necessary that he shall acknowledge his signature by some formal words as, "This is my will. I have already signed it."

63. *Sealing.*—Sealing is not usually necessary unless expressly required by statute. This requirement is made in Nevada and New Hampshire.

64. *Witnessing.*—In all the states except Pennsylvania attestation and subscription by witnesses are essential to the validity of a written will, unless the will is entirely in the testator's handwriting. See Art. **57.** The number of witnesses required differs in the various states. It is always well to have three competent and disinterested persons as witnesses, although in most states two witnesses are sufficient. The testator should sign the will before the witnesses, who should sign their names in the presence of the testator and of each other.

65. Persons witnessing a will should not be interested therein either as legatees, devisees, or otherwise. While the fact that a witness is interested in the will does not usually render the will invalid, it may disqualify him to take the portion which he would otherwise have received.

(D) A form of will.

66. A form of will is shown in Fig. 1 (*a*) and (*b*).

(E) Codicils.

67. A codicil is an addition to an existing will. It does not have the effect of revoking the will already made, but either supplements it or changes it in some particulars. It should be

expressly stated in the codicil that it is intended only to add to the will and not to revoke it. In general, a codicil should be executed with the same formality required in the case of wills.

(F) Revocation of wills.

68. A will may be revoked in various ways as follows: (1) by some later written will or other writing executed and

I, Edward Payne Brown, of the City of New York, County of Kings, and State of New York, being of sound mind, memory, and understanding, hereby revoke all former wills made by me, and make, publish, and declare the following as my last will and testament:

First. I direct that all my just debts and funeral expenses be paid as soon after my decease as may be done conveniently.

Second. I bequeath unto my brother, Arthur Brown, my library, my furniture, my watches and chains, my rings and other jewelry.

Third. I bequeath unto the Sanford Home for Indigent Widows the sum of Five Thousand Dollars ($5,000),

Fourth. I give, devise, and bequeath unto my sister, Celeste Brown, all the rest, residue, and remainder of my property, real and personal, wheresoever and whatsoever, to have and to enjoy the same during the term of her natural life.

Fifth. After the decease of my said sister, Celeste Brown, I give, devise, and bequeath one-half of the property heretofore given to her for life, to her lawful issue, and the other half to my brother, Arthur Brown, absolutely and forever, or in case he should die before her then to his lawful issue him surviving. If Celeste Brown should die without issue, then the whole to Arthur Brown and his lawful issue. If Arthur Brown should die without lawful issue, the whole to the lawful issue of Celeste Brown. Or, if both Celeste Brown and Arthur Brown should die without issue, the whole to my brother, J. Parsons Brown, absolutely and forever, or in the event of his dying before Celeste and Arthur, to his lawful issue him surviving.

Sixth. Should my said sister and brothers not survive me but die previously without leaving lawful issue them surviving, then I give all my said property unto the brothers and sisters of my late mother, Helen Janson Brown, or the issue of any of them who are now or may be then deceased, absolutely and forever.

FIG. 1 (*a*)

proved in the same manner as a will; (2) by the burning, cancelation, or destruction of the will by the testator himself or by some one else in his presence and by his express direction; (3) by words of revocation reduced to writing, read over, and

approved by the testator in his lifetime, with regard to wills of personal property in Florida, New Jersey, and Pennsylvania, and wills of personal and real property in Maryland and Ten-

Seventh. It is my wish that no portion of my estate shall go under any circumstances to any of my relatives on my father's side. They are to be excluded entirely from any participation therein, and what I may possess at the time of my death shall go only to my brothers and sister as aforesaid. Should none of my brothers and sister survive me, then to my relatives on my mother's side as hereinbefore provided.

Eighth. I appoint my brother, Arthur Brown, executor of this my last will and testament.

In witness whereof I have subscribed my name and affixed my seal hereto this eighth day of October, in the year of our Lord nineteen hundred and twenty-one.

[*Signed*] EDWARD PAYNE BROWN (SEAL)

We, whose names are hereto subscribed, do certify that on the eighth day of October, 1921, Edward Payne Brown, the testator, subscribed his name to this instrument in our presence and in the presence of each of us, and at the same time, in our presence and hearing, declared the same to be his last will and testament, and requested us, and each of us, to sign our names hereto as witnesses to the execution hereof, which we hereby do in the presence of the testator and of each other, on the said date, and write opposite to our names our respective places of residence.

[*Signed*] STEPHEN KENT,
Residing at New York, New York.
[*Signed*] RICHARD K. LYNCH,
Residing at New York, New York.

FIG. 1 (*b*)

nessee; (4) by a man's marriage and the birth of issue to him. In many states a woman's will is revoked by the mere fact of her subsequent marriage, without the birth of issue.

ESTATES IN TRUST

69. A trust is defined as a right of property held by one person for the benefit of another. The person who holds the property is called the trustee, while the person for whose benefit the property is held is called the *cestui que trust.* Usually a trust of real property can be created only by means of a

writing. A trust of personal property may be created by a writing or by word of mouth. The beneficiary, or *cestui que trust,* is not, strictly speaking, the owner of the trust property. The law recognizes a number of situations in which it is proper to make a provision for the benefit of certain persons, but to keep the actual legal ownership and control of the property out of them. This is done by appointing a trustee who holds the legal title, while the right to enjoy the proceeds or income from the trust property, called the equitable title, is lodged in the beneficiaries. A trust may be formed during the lifetime of the one who creates it by signing and delivering a deed of trust, or by a will taking effect after the testator's death.

(A) The various kinds of trusts.

70. *Dry Trusts.*—A dry trust exists where a trustee is given the legal title but has no active duties to perform. In many such cases no advantage is gained by depriving the beneficiary of the incidents of ownership. If A signs a deed conveying a farm to B in trust for C, and no reason appears in the deed of trust for creating a trust, the deed is not good as a trust deed, and an absolute title passes to C. C may take charge of the property and dispose of it as he pleases, and B has nothing to do with it. C is the beneficiary and there is no apparent need for B to interfere with the property.

71. *Active Trusts.*—An active trust exists where the trustee has active duties to perform, such as managing property. The purpose of the trust must not be unlawful. Such trusts are often created for the protection of the beneficiary in the expectation that the trustee chosen will be better able to manage the estate than the beneficiary himself.

72. *Spendthrift Trusts.*—Spendthrift trusts are recognized in many states. This kind of trust provides that the property shall be held by the trustee without liability to execution or attachment in any suit or for any judgment against the beneficiary and not subject to any disposition by the beneficiary by anticipation or otherwise. The beneficiary gets merely the net income, and he is protected against the consequences of his own prodigality.

PARTRIDGE v. CAVENDER, 96 Mo. 452 (1888). John Cavender by will gave property in trust for his son Robert S. Cavender for life, and directed the trustees to pay the income to Robert semiannually, "on his personal receipt therefor, without his said son having any power to sell, assign, or pledge the same previous to the payment thereof to him." Partridge rendered meritorious services to Robert S. Cavender in the preservation of the trust property and sued Robert and his trustee, Glover, in an effort to have the accrued income in Glover's hands applied to the payment of Robert's debt. *Held,* the testator's intention was that the income should be paid into the hands of his son to the exclusion of all other persons, whether claiming as assignees or creditors. Therefore, Partridge could not attach the accrued income until it had been paid to Cavender.

73. An intention to create a spendthrift trust must clearly appear. The words which are often used to denote such intention are as follows: "Provided that the trust estate hereby created shall not be subject to any attachment or execution against any of the beneficiaries or to any assignment or contract which the beneficiaries may make by way of anticipation or otherwise. Payments are to be made directly to the beneficiaries."

74. *Married Women's Trusts.*—A married woman's trust is one created for the sole and separate use of a woman, free from her husband's control. The intention is to protect the woman in the enjoyment of her separate property. Owing to the married women's property acts which generally give a married woman the same power over the property as if she were single, trusts of this character are of less importance than formerly.

75. If it appears that the woman to be benefited was neither married nor in contemplation of marriage when the trust was created, the trust fails and the woman may demand that the trustee deliver the property over to her absolutely and free from all trusts. Married women's trusts come to an end upon the death of either husband or wife.

(B) A trustee's powers, duties, and liabilities.

76. *To Execute the Trust.*—Usually the duties and liabilities of a trustee are defined by the instrument creating the trust.

The trustee should not depart from the terms of this instrument. He is not obliged to undertake the work and enter upon the duties of trusteeship, but once he does so he ought to carry out the terms of the trust faithfully, diligently, and with due regard to the beneficiary's best interests and the intentions of the creator of the trust.

77. *Investments.*—It is generally a trustee's duty so to invest trust funds as to obtain a reasonably high return without unduly risking the safety of the principal. Where the trust instrument does not designate the time when investments are to be made the trustee is allowed a reasonable time in which to invest.

78. The creator of a trust may indicate certain securities as proper investments for trust funds, or he may expressly prohibit the trustee from making certain kinds of investments. The statutes of most states designate certain forms of investment for fiduciaries. United States bonds, local, state, and municipal bonds and first mortgages upon improved real estate are usually safe investments for trust funds. A trustee is personally liable for losses resulting from his negligence or want of good faith. While he is not an insurer of the safety of funds placed in his hands, he is held to the exercise of a reasonable degree of sound business judgment.

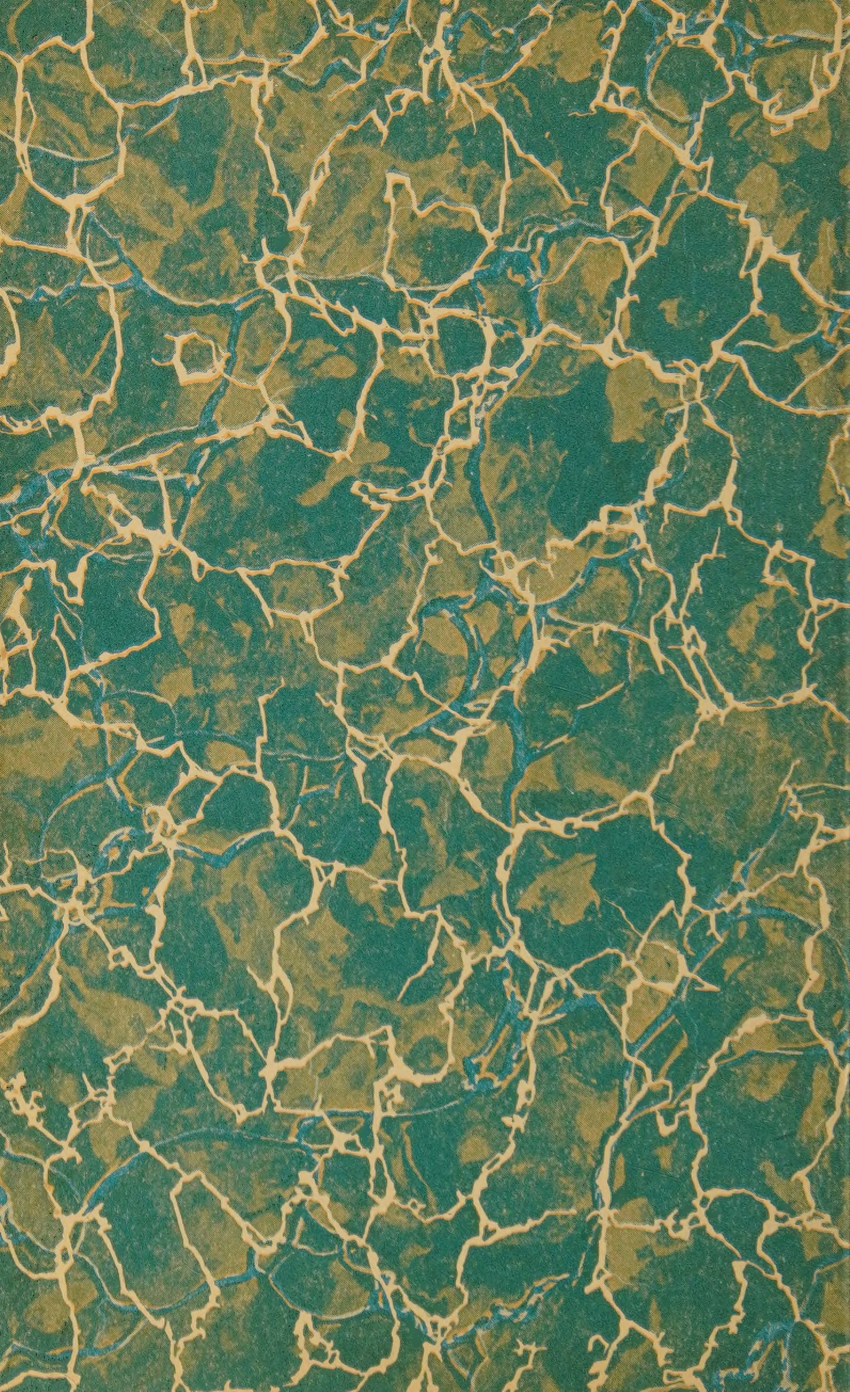
79. *Compensation.*—A trustee is usually entitled to a fair compensation for the faithful performance of his duties. His remuneration may be fixed by the trust instrument, or by some local rule of law may be based upon a percentage of the trust funds, both principal and interest, coming into his hands. Additional compensation may be allowed him when he has performed services other than those usually required in the administration of trust property.

80. *Accounting.*—A trustee should keep an accurate record of moneys handled by him, showing in detail all receipts and expenditures. The beneficiaries of the trust are entitled to have the trustee's accounts rendered to them periodically.

Sometimes the trust instrument or a local statute regulates the filing of the trustee's accounts.

81. The management of a trust estate may continue for years, and carelessness in any degree may result in heavy loss. The trustee should take receipts for all payments to beneficiaries and usually should not allow them to anticipate their income. If he does allow this, trouble may follow, because a life-tenant's income ceases when he dies. If the trustee has permitted a life-tenant to anticipate his income, the trustee will lose, for he cannot charge the remainderman with moneys advanced to the life-tenant.

82. It is the duty of a trustee to exhibit his books and accounts at reasonable times to those who have the right to inspect them. Where there are a number of beneficiaries each of whom is entitled to income, the trustee should not favor one at another's expense. His accounts should show how each stands as respects distribution of income and principal. He should also keep matters of distribution apart from matters of administration, the income account apart from the principal account, and the personalty apart from the realty account.



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